

AGREEMENT ON SHARE PARTICIPATION IN HOUSING CONSTRUCTION: HISTORICAL ASPECT AND LEGAL NATURE

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ABSTRACT

This article is relevant since legal regulation of shared construction participation is imperfect while the related legislation is renewed. In this regard, there was a demand for a comprehensive assessment of public relations arising in the context of shared construction participation and for defined legal essence of the contract that grounds the emergence of legal relations associated with shared construction participation. Methodology of research was based on analyzing domestic and foreign theoreticians in law especially Shared Construction Participation Agreement. This article draws a conclusion that an agreement regulating these relations is qualified as a separate, independent type of civil law contract, which main purpose is to protect the rights and interests of co-investors investing in housing construction by way of share participation.

Keywords: Building Owner, Shared Construction Participant, Investment Agreement, Contractor Agreement.

JEL Classifications: K11, K12, K34

INTRODUCTION

In Kazakhstan, shared construction institute was established due to prevailing economic situation. In the period of market economy formation (the 90s of the last century), building owners were granted credit on a very rare occasion since borrowing money from the bank was unprofitable due to huge credit interest. Secondly, not all banks were ready to provide construction loans. Those that decided to issue such a loan rarely offered an amount sufficient for the entire project. Thirdly, banks granting construction loans were aspired to take an active part as an investor. In other words, receiving an area in a constructed house was a compulsory condition (Abildinov, 2014; Mukhamadiyeva et al., 2017).

In this situation, building owners tried to find alternative methods for investing housing construction. At the beginning of 2000, this problem was resolved through a Shared Construction Participation Agreement. This fund-taking method had a number of advantages versus housing purchase in the primary market:

1. Progress payment (in most cases).

2. Housing purchase cost is lower than the market value of finished housing by 10-30% at share participation.
3. Prospects for shared construction participants in terms of their interest account at planning the habitable inner space (Zhumash, 2017).

At such construction financing, Construction Company's interest was that building owner takes the amount of finances required for successful construction by accumulating monetary contributions of shared construction participants on account of future housing purchase, thereby avoiding full or partial lending by financial institutions. In this regard, this agreement is beneficial for both the construction company and the shared construction participant.

Besides the positive characteristics, share participation in housing construction as a practice had many implementation problems over the years, since shared construction participants, deceived by unscrupulous building owners, could not get their housing. This situation has arisen when building was based on share participation in major cities of Kazakhstan in 2003-2006. This led to the problem of hoodwinked investors. For example, in contractual matters, this apartment could either belong to another person at the time of entering into the agreement, or be realized again later on. Shadow schemes, upon which Shared Construction Participation Agreement was replaced by a Purchase & Sale (P&S) Agreement, were often used to obligate the building owner to enter into principal P&S agreement after the construction. At the same time, unscrupulous building owner remained an object owner, who in turn could oblige the shared construction participant to pay a certain sum of money as a reserve or deposit before signing the principal contract while he/she has no right to demand payment, defined in the principal contract, under the presale contract (Slesarev, 2016).

As a rule, problems were related to the failure in delivering the project on time, building halt, contradiction between the construction quality and required standards, etc. There is a complete lack of the principle of good faith. In our opinion, account for legitimate interests and reasonable needs of participants is one of the good faith behavior criteria (Abdullah et al., 2015).

Since real estate has been increasing in price, construction period could be, at best, over a year. At the end, shared construction participant got the property much more expensive than the building owner promised him and was unable to pay for it.

At that time, the problem of hoodwinked investors arose due to a complete lack of legal regulation of these relations. Multi-family housing construction became shared in 2003 while the first Law of the Republic of Kazakhstan on Share Participation in Housing Construction was adopted on July 7, 2006, and entered into force on January 1, 2007 (The Law of the Republic Kazakhstan, 2006).

Currently, the State has claimed for unscrupulous building owners and their activity. Affordable Housing 2020 State Program was designed to protect the rights of shared construction participants. The Government of the Republic of Kazakhstan took measures to finance shared construction by the budget in the amount of KZT 263.4 billion (January 1, 2011). As a result, 450 residential estates (62,889 participants) were built at the beginning of world financial crisis in 2007. As of 2017, there were 12 problematic residential estates (over a thousand participants) (The Last Problematic Housing, 2017).

It should be noted that infusion of budgetary funds into shared construction is a one-off action caused by the need to prevent social tension.

Summarizing, relations of shared construction participation are not new for civil commerce and they were long present by the time the Law on Shared Construction was adopted.

Imperfect legislation, contradictions and gaps in legal acts on shared construction participation still generate problems in constituting contracts and lead to economic disputes. This situation arises due to assessment issues on legal nature of share participation in housing construction.

The purchase of residential estate under construction was registered by several contracts (Construction Agreement, P&S Agreement, Debt Settlement Agreement, Partnership Agreement, Investment Contract, Claim Assignment Agreement etc.) before the first Law of the Republic of Kazakhstan on Share Participation in Housing Construction was adopted on July 7, 2006.

There has been a controversy over the legal nature of Shared Construction Participation Agreement for a long time. Monographic research on legal regulation of relations in construction was written by Russian civilians on the basis of previous legislation. Therefore, it has lost its relevance. In Kazakhstan, only a few articles have been recently written on this problem. For example, Ilyasova K.M., Kazieva G. and Moroz S.P. were studying the issues of legal regulation of shared construction participation (Ilyasova & Kazieva, 2016; Moroz, 2011).

The purpose of this article is to analyze the legal nature of problems arising during the construction with funds taken from citizens and legal entities.

METHODOLOGY

The goal was achieved through the analysis of Kazakh law regulating the participation of individuals in shared construction in order to legally assess the Shared Construction Participation Agreement and determine its place in the legal system of Kazakhstan.

Analyzing various points of view on the legal nature of these relations, leading domestic and foreign theoreticians in law played a special role in the research. Methodological potential includes general (dialectical, analysis, synthesis, analogy, induction and deduction) and specific methods (systematic, linguistic, technical and comparative-legal) that allow comparing different views on the legal nature of relations arising during construction under share participation of individuals and legal entities.

RESULTS AND DISCUSSION

We have to draw our focus towards the history of this institution in order to understand the essence of shared construction participation as an independent institution of civil law.

It is still dubitable how the shared construction participation appeared for the first time there are different opinions on its origin. According to the first one, Shared Construction Participation Agreement was first signed in Brazil within the Affordable Housing State Program.

There is an assumption that this institution originated in Argentina in 1985 and was called Equitable Construction. The founder of this program was the President of Argentina Raul Alfonsin. At that time, Argentina was creating a very volatile economic situation, accompanied by hyperinflation and constant military conflicts. This financial crisis has entailed a situation when banks were not granting credits due to crash. The country needed stabilizing measures and economic reforms supporting citizens below the poverty line. Then the idea arose and then the Fair Housing Program was designed, which essence was that citizens could purchase housing on installment contract before the construction is finished. A special joint stock company was created to accumulate contributions from the population and provide shares equated to housing are in square meters. Raul Alfonsin managed to increase the number of homeowners from 2% to 21% (The Law of the Republic Kazakhstan, 2006).

The experience of shared construction participation began to be used in Chile, El Salvador and other countries of Latin America, Russia and Kazakhstan, as well as in a number of other countries that have used this experience in own peculiar way.

Equitable Construction was also borrowed by the United Kingdom, which distributed the practice in such countries as Egypt, the United Arab Emirates, Kuwait and Qatar. British companies did not create special joint-stock associations; they did sell not shares, but square meters of specific future housing. This was a guarantee of payback. This scheme proved to be effective, as confirmed by the experience of existing companies (Isabekova, 2015).

Currently, most European countries have already passed through a difficult stage of regulating relations arising during construction and developed their own concepts for real estate construction. In European countries, shared construction does not exist in the form that is used in Kazakhstan and Russia. In these countries, there is a contractual savings system that allows purchasing real estate during the construction. In France, for example, there is a system of deposit accounts (under 4% rates), according to which the future borrower accumulates a certain amount of money and claims a housing purchase loan. In Germany, this form is called construction savings banks.

In Europe, new homes market offers apartments in finished new buildings, sometimes even partially furnished. The European building owner is not going to sell square meters to retail buyers during the construction, since this requires marketers, salesmen and other employees who must be paid (International Construction, 2015). Large investors, however, could buy them, as they are buying at least 1/3 of apartments in a high-rise building. Hans-Joachim Schramm, the assistant professor at the University of Bremen, writes that payment plan might be like this: 30% of value is paid before purchasing land and starting construction; 40% should be paid after the building with unfinished surface is done; then 10% afterwards, after the roof and installations are ready, and the building is ready for occupiers (according to the decree on third and contracting companies) (Schramm, 2017).

The buyer also has no benefit from buying an apartment in a new building, sine banks grant loans at 4% interest for finished apartments, but can refuse to grant mortgage in case of building being under construction.

Hence, credit granting system without risks to the borrower exists under stable economy.

There are different points of view on the legal nature of Shared Construction Participation Agreement. The main reason for these disputes is that Kazakh legislation did not contain special rules governing this type of contract. At that time, basic legal sources regulating these relations involved the Civil Code of the Republic of Kazakhstan and the Law of the Republic of Kazakhstan on Housing Relations that did not regulate the composition and legal status of participants completely.

Currently, the Law on Share Participation in Housing Construction (October 7, 2016) contains 7 articles regulating the form, amendment and termination of Shared Construction Participation Agreement, as well as rights and obligations, responsibility of parties, and transfer of shares (The Law on Share Participation in Housing Construction, 2016). Unfortunately they do not disclose the legal essence of agreement. Therefore, there are still disagreements on this issue.

Thus, Zhuravleva A.A. argues that in domestic legal order, real estate purchase transactions at the stage of construction are mediated by investment contracts (Zhuravleva, 2016).

Ilyasova K.M has a similar opinion. According to her, availability of assessment provisions implemented to assess the grounds for legal relations arising at investing is the main point for determining the scope of the Law on Share Participation in Housing Construction (Ilyasova & Kazieva, 2016).

The opposite point of view is held by the authors, who do not agree with the approach towards determining the investment nature of Shared Construction Participation Agreement. According to Arapaeva S.S., shared construction cannot be regarded as an investment activity. Firstly, investment and share construction are regulated by different legislation. Secondly, investor's goal, as well as the purpose of the investment project, is to make maximum profit (Arapaev, 2014).

Investment contract is aimed at an effective investment. The economic nature of investments is that specific monetary contributions are made to profit-making areas, thereby ensuring financial enrichment. Housing construction can be viewed as an investment activity if this activity is entrepreneurial for the investor. Currently, investment activity is regulated by the 25 Chapter of the Entrepreneurial Code of the Republic of Kazakhstan, according to which any objects and types of entrepreneurial activity are objects of investment activity, except for cases provided for by the Laws of the Republic of Kazakhstan (The Entrepreneurial Code of the Republic of Kazakhstan, 2017).

As a rule, shared construction participants enter into agreement to satisfy own housing demands, for example to improve housing conditions. Therefore, apartments purchased by participants are not objects of their investment activity.

Kratenko M.V. is sure that contractual relations of shared construction participation are regulated by the Law on Protection of Consumer Rights, since the Shared Construction Participation Agreement is settled to fulfill the housing demand. This statement can be questioned in terms of parties. The matter is that participants can be both individuals and legal entities, according to the Law of the Republic of Kazakhstan on Share Participation in Housing Construction, while the consumer can only be an individual (Kratenko, 2010).

Shaydullin R.R. argues that this agreement is more in a line with the construction agreement while the civil regulation of contracting institution is most suitable for regulating the relations of shared construction participation (Shaydullin, 2016).

This position is controversial, since these two contracts differ in the subject matter. According to the Construction Agreement, contractor creates the object and entirely transfers it to the project owner (Paragraph 1, Article 651 of the Civil Code of the Republic of Kazakhstan). According to the Shared Construction Participation Agreement, finished real estate is not transferred to the investor entirely he/she receives only the share that was ordered and paid, and must be received from the contractor (The Civil Code of the Republic of Kazakhstan, 2017).

As a rule, participant does not give the building owner the task, but chooses an object from those that the building owner offers. Very often, real estate as a subject of Shared Construction Agreement is built regardless of the Agreement on Share Participation. Therefore, participant can enter by making a monetary contribution at any stage of construction.

Features typical for the Construction Agreement are that the project owner is obliged to timely provide the contractor with a land plot of area and condition specified in the contract (Paragraph 1, Article 658 of The Civil Code of the Republic of Kazakhstan). As a rule, such a land plot must be purchased by the project owner. In addition, project owner is obliged to transfer to the building owner the engineering survey data, project documentation and construction permit. According to Kazakh law, real estate ownership automatically leads to the

emergence of land ownership. In Russia, for example, land can be owned by one citizen or legal entity while the object built on it is owned by another citizen or legal entity (Larisa et al., 2015).

As for the Shared Construction Participation Agreement, building owner must have a land plot for construction as a property or own it on any other land use right; special-purpose company must have a building license as and when required issued by the State Architectural and Construction Control Authority. At the same time, there are relations arising between the building owner and the special-purpose company in the field of technical documentation that can be drawn up in a particular contract with or without alienation of exclusive rights to technical documentation in favor of the building owner.

Based on the relations of shared construction participation, it is assumed that a building owner must have construction documents and positive report on State appraisal before signing an agreement with the first participant.

Shared construction participants do not have rights and obligations of the building owner and the project owner provided for by the Civil Code of the Republic of Kazakhstan. In particular, participant: (1) does not introduce changes into the technical documentation; (2) does not control and supervise the progress and quality of construction, as well as the quality of materials. Generally, participants do not regulate construction and the builder does not have to act by participant's order.

Shared Construction Participation Agreements and Construction Agreements are settled by parties:

1. Building owner undertaking to start building high-quality housing at contractual date.
2. Shared construction participant entering into a bank account agreement and undertaking to put money on a deposit and to take a share in a residential building if commissioning certificate is available.
3. Special-purpose company undertaking to build a residential real estate on contractual time, obtain a commissioning certificate and transfer to the participant his (her) share.
4. Agent bank, which duty is to accept participant's deposit with an interest charge.

Subjects of the Construction Agreement are: project owner and contractor. These could be any individuals and legal entities with special knowledge and skills in the field of construction. Principal contractor and subcontractor are commercial construction companies. These subjects perform building operations with a license for certain types of construction activities.

As for the Shared Construction Participation Agreement, building owners must have a license for shared construction (may be a legal entity). Shared construction participants can be individuals and legal entities.

Another difference between these agreements is that if the project owner has an interest in estate at contract termination (Construction Agreement), then a participant shall have a compulsory repayment claim with interest.

Summing up, Construction Agreement and Shared Construction Participation Agreement are not identical contracts, since their only common feature is that they both regulate housing construction, but legal relations are different in legal nature.

There is another point of view on the legal nature of Shared Construction Participation Agreement, according to which it is a Partnership Agreement. At no legal regulation of relations arising from share participation in housing construction, they suggested to apply the rules of partnership. This became especially relevant when there were problems based on long-term construction or skullduggery.

This legal situation was criticized. Such scholars as Em V.S. and Kozlova N.V. noted that relations between participants and building owner are registered not only by a multilateral agreement, but by various agreements. The legal approach to registration is usually individual for every participant. Thus, each Shared Construction Participation Agreement is settled with due account for case peculiarities. General characteristic of all relations arising during the construction cannot be given as one package contract (Em & Kozlova, 2014).

In our opinion, this criticism is very correct. Besides, contracts Shared Construction Participation Agreements cannot be replaced with Partnership Agreements, since building owner needs only participant's investments and participant does not take part in construction management or contract settlement with third parties. Thirdly, participants and building owner have different goals: buying real estate for personal needs and getting profit, respectively.

Isabekova Zh.I. has determined the types of Shared Construction Participation Agreements depending on party's consumer and commercial. She has noted that Shared Construction Participation Agreement is a hybrid contract that includes elements of the Construction Agreement; Real Estate Sale Agreement; Commission Agreement; Agreement on Investment Unit. According to her, it is peculiar due to parties, subject matter, material term, specific organizational and legal prerequisites (building license and project declaration availability) (Isabekova, 2015).

Moroz S.P. has a similar opinion. He identified the agreement as a hybrid contract that can have two basic forms agreement on share participation in housing construction settled for consumers (consumer contract regulated by the Law of the Republic of Kazakhstan on Protection of Consumer Rights) and agreement on share participation in housing construction settled for business purposes (commercial contract; accordingly, risks under this contract are carried by the entrepreneur) (Moroz, 2011).

There is an opinion that Shared Construction Participation Agreement has to be considered as an independent type of civil contract while determining its legal nature. Thus, Zhumagulov writes we should recognize the independent nature of the Shared Construction Participation Agreement, although it is probably similar with civil contracts. Legal comparison with other contracts leads to a delusion and new opposing opinions. Thereby, there is no single theoretical position in the system of civil law relations (Zhumagulov, 2014).

Theoretically and legally analysis the existing Kazakh legislation and scientific interpretation of legal categories in the field of shared construction allows drawing the following conclusions.

Firstly, the Law on Share Participation in Housing Construction is adopted to solve the problems of raising funds for shared construction and proper legal regulation of relations between parties under the terms of related agreement.

Secondly, we can trace the principle of weaker party protection in relations the Law on Share Participation in Housing Construction. In this regard, the main purpose of the Shared Construction Participation Agreement is to protect the rights and interests of individuals and legal entities that invest in housing construction in the order of share participation.

Thirdly, the legislator seeks to ensure the transparency of construction business by providing for compulsory information release by the building owner (about himself and the real estate).

Despite the fact that the Law on Share Participation in Housing Construction adequately regulates the contract settled between the building owner and shared construction participants,

and is the legal basis for shared construction, this Law adopted in 2016 did not make the problem of assessing the Shared Construction Participation Agreement less relevant.

Analysis of contracts provided for by the Civil Law allows concluding that the Shared Construction Participation Agreement is not related to any of them.

Moreover, this agreement cannot be called hybrid, since it does not contain elements of contracts provided for in legislation. In this case, these elements should be understood not as specific rights and obligations, but as a certain set of them typical for the relevant contract.

For example, Shared Construction Participation Agreement has no grounds for including elements of the P&S Agreement as they have different subject matter.

Legal characteristic defines that the Shared Construction Participation Agreement is bilateral, consensual and paid. This contract cannot be classified as public, but it is an adhesion contract. Contract's main feature is the form availability used to close transactions consummated in mass quantity. This corresponds to the essence of the Shared Construction Participation Agreement (The Order of the Minister of National Economy of the Republic of Kazakhstan, 2016).

There is disclosed historical aspect of the legal regulation of relations in shared construction, analyzed views of researchers on investment and civil law, and arguments that either dispose or confirm their validity.

CONCLUSION

The Shared Construction Participation Agreement has the following typical features that allow assessing it as a specific independent civil contract: the specific features of the subject matter; specific parties; various goals of different parties; material term stipulated by the Law on Share Participation in Housing Construction; large number of compulsory rules related to the fulfillment of building obligations; state registration of the contract and its additions and changes, as well as the assignment of claims.

Relations of shared construction participation should be regulated primarily by civil legislation. In this case, there should be a new type of civil contract captured in the Civil Code of the Republic of Kazakhstan agreement on share participation in housing construction that would help to reduce the risks of shared construction participants and increase the attractiveness of such a housing solution as citizen participation in multi-family housing construction.

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