



POLICY BRIEF # 4
OCTOBER, 2023



THE PHOENIX
COMPANY
CHRONICLES:

KAINDA CABLE FACTORY ASSET TRANSFER TO 'METALL-KEN' LLC

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One of the most significant obstacles for foreign investors entering brownfield investments in Kyrgyzstan is the questionable ownership status of various production facilities. This issue arises from the chaotic privatization of post-Soviet assets, coupled with the concealment of beneficial ownership practices and limited asset recovery efforts pursued by authorities following subsequent revolutions. The transformation of the Kainda Cable Factory faced these challenges, and although not without controversies, its facilities escaped a 'rusty fate' thanks to the engagement of a Chinese investor and were reborn as 'Metall-Ken' LLC.

ABOUT THE AUTHOR

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INTRODUCTION

On 17 May 2018 the shareholding structure of OJSC Kainda Cable Factory (ros. ОАО Каиндинский кабельный завод) was announced where along the State Property Management Fund (ros. Фонд по управлению государственным имуществом, FUGI) (24,79%) new shareholders were indicated - Aibek Turdubaev (42,24%) and Raimbek Abdymalikov (24,82%) [1]. Following, on 24 July 2018, a shareholders' meeting was held where new majority shareholders, in the absence of FUGI, approved the transfer of factory assets to the company 'Metall-Ken' LLC (rus. Общество с ограниченной ответственностью 'Металл-Кен') in a debt settlement agreement [2]. As a result, OJSC Kainda Cable Factory was effectively stripped of all its assets and became a non-viable entity. On the other hand, 'Metall-Ken' LLC could be characterized as a phoenix company, where assets of an insolvent dormant company (OJSC Kainda Cable Factory) were transferred to renew business activities as a new legal entity.

The situation led to the attention of public opinion as reportedly, on the eve of the loan settlement agreement on 6 July 2018, the Chinese investor - Fujian Taihao International Trade Company (FTITC) (ros. Фуцзяньская международная торговая компания 'Тайхао') acquired ownership in 'Metall-Ken' LLC from Kyrgyz owner - Gulsara Kanybekovna Sulaimanova (ros. Сулайманова Гулсара Каныбековна) [3].

POLITICAL CORRUPTION ALLEGATIONS

In January 2021, the journal 'PolitKlinika' published the results of a journalistic investigation pointing to the presence of political corruption in the process of Kainda Cable Factory's asset acquisition. The investigation underlined that Gulsara Sulaimanova, the Kyrgyz co-owner of 'Metall-Ken' LLC, is the ex-wife of former lawmaker Aliyarbek Abzhaliyev. Furthermore, it was alleged that the new shareholders of Kainda Cable Factory were her close relatives. Aibek Turdubaev is reportedly her sister's husband, and Raimbek Abdymalikov is her brother. Thus, it could be stated that the asset transfer to 'Metall-Ken' LLC could be seen as proxy voting done by affiliated persons [4].

The investigation indicated that by August 2018, most of the production assets of Kainda Cable Factory had been successfully transferred to 'Metall-Ken' LLC, and reportedly the debt settlement was accepted by Crannet Corporation, an offshore company registered in the British Virgin Islands, which reportedly owned the claim rights to Kainda Cable Factory's debt. However, the asset transfer did not include the main production building, which was owned by another Chinese-owned company, 'Target Kompanii' LLC. In a strange coincidence, in April-May 2018, the property was confiscated by state authorities, and the owners of Target Company were arrested by the Kyrgyz State Committee for National Security (GKNB) as part of an operation against Value-added tax (VAT) fraud [5].

This enabled 'Metall-Ken' LLC to directly acquire the desired property from the state.

It raised controversy that actions against 'Target Kompanii LLC' were allegedly influenced by Aliyarbek Abzhaliyev. This allegation is indirectly confirmed by the fact that, in March 2021, criminal case proceedings were launched against him in line with Article 308-1 "Illicit enrichment" of the Criminal Code. GKNB commented that "Abzhaliyev lobbied for the interests of private structures to the detriment of public ones. While working in public positions, he acquired property assets that are incomparable with his official income." In his case, an important pressing factor on state bodies was allegedly his kinship with ex-president Sooronbai Jeenbekov. Abzhaliyev admitted his guilt, and in accordance with the economic amnesty introduced by the new President Sapar Japarov, he was not arrested and even retained his parliamentary mandate after paying compensation to the state [6].

CHINESE INVESTOR AND TROUBLED ASSETS PROBLEM

During its heyday, the Kainda Cable Factory, founded in 1958, proudly produced a remarkable 15 thousand tons of enameled wires annually, supplying its high-quality products to a wide expanse of the Soviet Union [7]. However, as of 2016, production at the factory was halted, and it was a loss-making one [8]. The factory's problems were additionally aggravated by its unclear ownership structure.

In 2013, the State Property Management Fund (FUGI) confirmed that they could not explain how state ownership in the company was lowered from 60.05% in 2004 to 24.79% in 2013 due to missing documents [9]. Moreover, the remaining ownership was largely fragmented in the hands of more than a thousand shareholders. Thus, the assessment of OJSC Kainda Cable Factory suggests that it qualifies as a distressed asset, raising concerns about its investment viability.

Still, Kyrgyz authorities regularly underlined their will to revitalize the factory with the help of foreign investors and repeatedly informed about expressed interest from Chinese companies to revitalize cable production or re-profile the enterprise [10]. Reportedly, in 2017, Fujian Taihao International Trade Company approached state authorities, including the Agency for the Promotion and Protection of Investments of the Kyrgyz Republic (APZI), and expressed its interest in acquiring the Kainda Cable Factory production assets. However, it chose to collaborate with 'Metall-Ken' LLC in the acquisition process of OJSC Kainda Cable Factory's assets. It should be noted that in response to the investigation by 'Politklinika,' the Chinese investor underlined the legality of the asset transfer and distanced themselves from alleged politically-backed support. Furthermore, the Chinese investor stated that they are willing to buy the remaining state's shares in OJSC 'Kainda Cable Factory' from FUGI to settle any further claims [11]. Finally, it should be stated that the investment of the Chinese

investor and their ownership rights were not questioned by state authorities after the 2020 revolution. In November 2020, the then-Deputy Prime Minister paid a visit to 'Metall-Ken' LLC, assuring state protection and support for the investment [12]. Therefore, we could assume that the potential claims from FUGI were solved, and public interest secured. In June 2021, it was reported that the factory started operations in line with its new profile. The company now produces different types of fittings, and its production capacity is 300 thousand tons of metal products per year. Furthermore, APZI recognized the investment amounting to 50 million USD as one of the flagship investments of the 2021 year [13].

RECOMMENDATIONS

1. Development of Clear Policies Regarding State Asset Recovery and Transformation Procedures of Dormant Companies:

Establish well-defined policies governing the recovery and transformation of dormant state-owned entities, prioritizing the protection of both private and public interests. "Metall-Ken" LLC could be described as a successfully operating phoenix company, and at large identify Chinese capital as a constructive force supporting a legally conducted phoenixing process of a dormant company (Kainda Cable Factory). Such procedures could mitigate the direct and indirect involvement of politically exposed persons (PEP).

2. Vigilance Against Bankruptcy Fraud:

While recognizing this case as a legitimate phoenixing process, it is imperative to raise concerns among state authorities regarding the escalating risk of bankruptcy fraud. This risk is associated with practices such as debt restructuring, asset transfer/stripping, and the potential presence of highly detrimental forms of bankruptcy fraud, including the "bleed out" type, within the Kyrgyzstan landscape [14].

3. Development of an Effective State Mechanism for Brownfield Investment:

To foster brownfield investment successfully, a robust and efficient state mechanism is indispensable. The case underscores the inefficiencies of the current mechanisms, which have given rise to potential issues and allegations against foreign investors. It underscores the need to prevent the privatization of foreign investor engagement and emphasizes the importance of seamless coordination among state agencies responsible for national asset management and investment attraction. The case highlighted risks for investors stemming from 'political capture,' particularly in the ever-evolving landscape of Kyrgyzstan, where political influences can disrupt business decisions and operations.

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DISCLAIMER:

The analysis and recommendations presented in this policy brief are based on data and conditions as of March 2023. While every effort has been made to ensure the accuracy and relevance of the information, circumstances may have changed since that time.
