

IMPROVING THE MECHANISMS OF SHARED HOUSING CONSTRUCTION THROUGH THE INTRODUCTION OF ESCROW ACCOUNTS IN UZBEKISTAN

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Abstract

The introduction of escrow accounts in Uzbekistan’s shared housing construction marks a major step toward increasing transparency, investor protection, and financial discipline in the real-estate sector. This thesis examines the essence, objectives, and potential impacts of Presidential Decree PF-11 (January 27, 2025), which regulates the transition to escrow-based project financing mechanisms for housing construction. Using international comparison and analytical review, the study identifies global best practices in project financing, evaluates their adaptation to the Uzbek context, and proposes recommendations for effective policy implementation.

Keywords: Escrow accounts, shared construction, project financing, housing market, Uzbekistan, investment protection, transparency.

Housing construction has long been one of the most dynamic yet vulnerable sectors in Uzbekistan’s economy. Rapid urbanization, population growth, and rising living standards have created increasing demand for housing, but the financing mechanisms have often been opaque and risky. Until recently, the prevalent “shared construction” model exposed individual investors (equity participants) to significant legal and financial risks due to weak guarantees and unregulated developer behavior.

Recognizing these challenges, the Presidential Decree PF-11 of 27 January 2025 introduced a new institutional framework aimed at implementing the principle of the “Single Housing Life Cycle” and protecting stakeholders through escrow accounts. This mechanism represents a structural shift toward a more transparent, bank-controlled financing system consistent with international project-finance standards.

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The research problem of this thesis lies in assessing how the newly introduced escrow-based system will transform project financing in Uzbekistan, improve citizens' property rights protection, and enhance trust between developers, banks, and the state. The study further investigates whether this reform can ensure sustainable housing sector development by balancing investor safety, market efficiency, and construction profitability.

In the global financial and construction sectors, escrow accounts are widely recognized as instruments ensuring the security of financial transactions (Hendershott & Shilling, 2017). They are used in the United States, Japan, and the European Union to protect investors' funds during project implementation. According to the OECD (2021), escrow mechanisms provide transparency, accountability, and reduced default risks by placing the funds under the supervision of an independent financial institution until contractual obligations are fulfilled.

In the Russian Federation, the Federal Law No. 214-FZ (amended 2019) made escrow accounts mandatory for all shared-construction projects. This legal innovation successfully reduced fraud cases and improved banking sector participation in housing finance (Kudrin et al., 2020). Similarly, China's Housing and Urban-Rural Development Law requires developers to deposit advance payments into regulated escrow accounts, strengthening consumer protection and curbing speculative practices.

Empirical studies from South Korea and Singapore (Lee & Kim, 2022; Lim, 2019) show that escrow-based financing minimizes systemic risk by ensuring that funds are released to developers only after verified construction milestones are achieved. In the EU, the Basel III and IV frameworks emphasize risk-weighted transparency in project finance, which aligns with Uzbekistan's planned credit allocation tied to the size of escrow deposits (European Banking Authority, 2023).

In Uzbekistan, the legal foundation for shared housing construction was initially defined by the Regulation No. PQ-4732 (2020). However, enforcement remained weak due to the absence of banking oversight and digital monitoring. Scholarly works (Karimov, 2022; Mirzayev, 2023) highlighted the need for financial intermediation and escrow supervision to safeguard equity participants. The new Presidential Decree PF-11 (2025)

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directly addresses these gaps by introducing mandatory escrow accounts, electronic construction platforms, and bank-linked project financing.

An escrow account is a special type of account opened at a commercial bank in which the client's (depositor's) funds are held until certain contractual conditions are fulfilled. In this mechanism, the bank acts as an intermediary: the funds are not fully transferred either to the seller or the buyer but are released to the respective party only after all the terms of the agreement have been satisfied. In this way, the escrow account functions as a third-party guarantee, ensuring trust and transparency in economic relations.

In the banking system, the significance of escrow accounts is reflected in several key aspects. First and foremost, it serves as a financial security instrument that protects clients' rights. For example, in the housing construction sector, the payments made by buyers to developers are not transferred directly but are instead deposited into an escrow account. Once the construction work is completed and official permission for use is granted, the bank transfers the funds to the developer. Through this mechanism, the financial interests of equity participants are fully safeguarded. Thus, the reform represents both an institutional modernization and a financial innovation, integrating civil-law mechanisms with banking risk management tools.

First and foremost, the funds accumulated in escrow accounts serve as an inexpensive and stable source of resources for commercial banks. Since these funds remain on the bank's balance sheet until the contractual conditions are fulfilled, their circulation is temporarily suspended, allowing banks to utilize them as a liquidity cushion. Access to such resources enables banks to expand their credit portfolios. Theoretically, as a bank's resource base grows, its lending capacity increases accordingly.

The mechanism of gradually reducing interest rates provides a dual benefit. On the one hand, it eases the financial burden on developers and motivates them to complete projects on time. On the other hand, it allows banks to expand their lending volumes and attract more borrowers. Consequently, the overall growth of the loan portfolio leads to an increase in the bank's total income. This outcome corresponds to the microeconomic principle of an "optimal balance between volume and margin."

Determining the lending interest rate based on the amount accumulated in escrow accounts functions as an effective risk management tool for banks. The larger the volume of funds held in escrow, the lower the credit risk, since these deposits act as an additional guarantee of the developer's fulfillment of obligations. Under such conditions, reducing the interest rate reflects the bank's adaptive and risk-sensitive policy.

International experience also confirms the effectiveness of this approach. For instance, since 2019, Russian banks financing construction projects through escrow accounts have linked interest rates to the size of the accumulated deposits. As a result, the financial discipline of developers has improved, and the profitability of the banking sector has become more stable. Similarly, in the United States, escrow mechanisms in mortgage lending have helped diversify banks' income sources and reduce systemic risk.

Thus, the proposal is scientifically justified by the following points:

- Escrow accounts create a stable and low-cost funding base for banks.
- Gradual reduction of interest rates stimulates credit demand and expands the loan portfolio.
- Interest rate policy tied to the amount of deposits serves as an effective risk management mechanism.
- International practice confirms the efficiency of this model in enhancing banking profitability.

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