Kazakhstan

Foreign Investment in the Oil and Gas Sector of Kazakhstan

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A foreign company may carry out its activities in the Kazakhstani oil and gas sector either through a branch or a locally registered company.

A "locally registered company" means a company registered in the Republic of Kazakhstan which can be 100% foreign-owned, but which would still be considered a Kazakhstani enterprise for the purposes of the laws regulating the oil and gas sector; as opposed to a branch office, which is a subdivision of a foreign company and not a separate entity.

Generally, the current Kazakhstani legislation contains no limitation for foreign entities to participate (through their branches) in tenders for the provision of goods and services associated with oil and gas operations. The relevant state authority supervising such tender as well as the tender committee are not required and/or entitled to refuse the participation by a foreign company in a tender on the ground that it is not established in Kazakhstan. Thus, as per the current legislation, all bidders in tenders, both Kazakhstani and foreign, are subject to the same bidding procedures, and terms and conditions of bidding in any tender.

However, under the legislation, Kazakhstani enterprises have a certain priority when bidding in tenders. Yet, the nature of such priority has not been clarified by the regulations. There may well be certain practical implications of such "priority" at the stage of choosing a winner, while, for example, deciding between equal tender proposals of a Kazakhstani and foreign company, both meeting the requirements and conditions of the tender. However, currently, no laws or regulations contain such recommendations, guidelines or provisions.

Another point to note is that should the tender bids of foreign companies be equal, then preference in choosing the best bid should be given by the tender committee to those bidders which: **(i)** produce their works, goods and services on the territory of the Republic of Kazakhstan; **(ii)** attract modern technology into Kazakhstan; **(iii)** use goods, works and services supplied by Kazakhstani enterprises; and **(iv)** offer to use foreign goods, works and services through a joint venture where the Kazakhstani enterprise's share will be at least 50%.

Therefore, by having registered a 100% foreign-owned company in Kazakhstan, a foreign company would be in a better position to constitute the Kazakhstan content of purchased works and services of general contractor firms, although there are further qualifications as to what that content should be.

The most suitable form of a Kazakhstani company is a Limited Liability Partnership ("LLP").

Below we give a brief explanation of the concepts of a branch office and LLP under Kazakh law, the main distinctions between these two (2) and we also outline certain issues pertaining to the registration of each of a branch office on the one hand and an LLP on the other, currency regulations and the applicable tax treatment.

Legal Status

Of course, a branch of a foreign entity is not treated as a separate Kazakhstani legal entity but represents and constitutes an integral part of the foreign legal entity in Kazakhstan. A branch is a subdivision of a foreign entity, which may fulfil all or a part of the functions of its parent company, including income-generating activities. A branch office acts on the basis of a "Regulation" (similar to a charter or by-laws), and is typically managed by an individual authorised by the parent company and acting pursuant to a power of attorney.

A branch acts and assumes obligations in the name of the founding entity.

LLP is a separate legal entity acting in its own name pursuant to a charter approved by the founders/participants. An LLP is formed on the basis of contributions from its participants and such contributions form the LLP's Charter Capital.

Liability

The participants in an LLP are not liable for the LLP's debts and bear the risk of losses arising out of the LLP's activity to the extent of the value of their contributions. An LLP is liable for its debts to the extent of all its assets and is not liable for the debts of its participants.

Where litigation is brought in a Kazakhstani court, a Kazakhstani legal entity can be a defendant. However, since a branch office is not a legal entity per se, of course, the parent company itself would be named as the actual defendant. In practice, Kazakhstani courts commonly reject a claim if it is brought against a branch office and not its parent company.

Management

A branch manager has to be appointed by the authorised body of the parent company and typically operates on the basis of a power of attorney. Within the powers granted by such power of attorney, a branch manager may appoint other management/ administrative personnel of the branch.

An LLP is managed by a general meeting of participants and its executive body (director, management board). An LLP's Charter may also provide for the formation of a supervisory body and/or audit commission.

Charter Capital

Since a branch is not treated as a separate legal entity, there are no legal requirements to maintain the charter capital of a branch.

To get an LLP registered, the founders have to form the charter capital, which currently may not be less than 87,200 Kazakhstani Tenge (approx. US$590).

Currency Regulation

For currency regulation purposes a branch of foreign legal entity is not considered to be a resident of Kazakhstan whereas an LLP is such a resident. A branch, being a non-resident, is entitled to make payments in foreign currency to both residents and non-residents of Kazakhstan, while an LLP has to make payments to residents in Kazakhstani currency only, with some exemptions established by the legislation.

An LLP may purchase foreign currency for certain purposes listed in the relevant legislation, like payments to non-residents or repayment of loans extended by an authorised bank. In contrast, a branch can purchase foreign currency for any purpose.

Currency transactions involving the movement of capital from residents to non-residents (which include investments by residents abroad, payments of residents to non-residents in relation to import transactions providing for advance payments for goods (work, services) for a period in excess of 180 days and some others) must be licensed by the National Bank. If a Kazakhstani legal entity wants to open an offshore account, it will require a license to be issued by the National Bank of the Republic of Kazakhstan.

Tax Treatment

A branch of a foreign legal entity and an LLP are treated similarly for tax purposes. The only difference is the nature of taxes paid and method of tax collection. A branch is subject to a 15% net profit tax on its after-tax income as earned or accrued. This tax is essentially the same as the 15% withholding tax that applies to dividends distributed by a Kazakhstani legal entity. However, the ability of the Kazakhstani legal entity to retain its earnings without paying withholding tax until the earnings are actually distributed is the principal difference between the application of withholding tax to the distributions by an LLP and the branch profits tax, attributable to the net after–tax income of a branch. On the other hand, a branch office is required to pay tax on its profits when they are earned (i.e. on the date established by the tax laws for payment of profits tax), which lends a slight advantage to using an LLP instead of a branch. Furthermore, the relevant Double Tax Treaty to which the Republic of Kazakhstan is a party may reduce the rate of withholding tax on dividends.

With the distinctions described above, both a branch and LLP are subject to the following main taxes:

1. **Income Tax,** accrued with respect to the income to be calculated as the difference between the aggregate annual income and all and any applicable deductions. The regular income tax rate is 30%;
2. **Value-added tax (VAT) at 16%** calculated with respect to taxable supplies and services in Kazakhstan and imports.
3. **Social Tax at 21** % for resident employees and 11% for non-resident employees;
4. **Land Tax** with respect to any land plots owned by a branch/LLP. It is calculated on the basis of annual fixed payments for a unit land area. The basic rates are subject to a co-efficient established annually by the Government of Kazakhstan;

5. **Property Tax** applies with respect to the residual value of depreciable assets. It is paid annually at a rate of 1% of the value of any depreciable assets;
6. **Vehicle Tax** is assessed with respect to vehicles owned by the LLP. It is paid once a year and is calculated on the basis of engine capacity and year of production of the vehicle.

Registration Procedures

There are some minor differences in the registration process for a branch and for a legal entity, particularly regarding the documents, which must be filed with the Ministry of Justice. (There are also some differences in the filing requirements for a branch office and for an LLP).

The incorporation of an LLP or a branch in Kazakhstan requires registration with the Ministry of Justice (or City/Oblast Department of Justice), the Statistics Department and the Tax Inspectorate.

Registration fees payable for such registration currently amount to KZT 17,440 (approx. US$118).

Granting of Investment Preferences in the Republic of Kazakhstan

The first decade of existence of independent Kazakhstan is characterized by the influx of investments of considerable volume (both foreign and kazakhstani) to the different areas of the economy of the Republic of Kazakhstan. Kazakhstan is high on the list of Central Asian countries according to the amounts of investments, especially in the oil & gas area.

During a long period of time the activity of investors in Kazakhstan was regulated by the Law "On Foreign Investments" and Law "On State Support of Direct Investments" which became invalid on January 8, 2003 because of adoption of a new Law of the Republic of Kazakhstan "On Investments".

The new Law made alterations to the procedure of granting the preferences to the investors who invest in the priority sectors of economy of the Republic of Kazakhstan.

First of all consideration must be given to the fact that in contrast to the previous Law "On Foreign Investments" the new Law does not include at all the concept of investment benefits. The legislation provides only for the grant of **investment preferences** to the legal entities of the Republic of Kazakhstan who realize the investment project.

The kazakhstani legal entity who realize the investment project is entitled to get the following investment preferences (hereinafter referred to as "preferences"):

1. Tax preferences

2. Exemption from customs duties

3. State natural grants

The investment preferences are granted provided the compliance with the following main conditions:

1. The investments are made to the priority sectors of economy of the Republic of Kazakhstan, the list of which is approved by the Government of the Republic of Kazakhstan;

2. The investments are made to the fixed assets of legal entity of the Republic of Kazakhstan, at that the new productions are created, expanded and renewed with use of modern technologies.

The additional conditions for granting different types of preferences are given bellow.

The investment tax preferences

The investment tax preferences are granted in the form of:

1. Vesting the taxpayer with a right to make additional deductions from his/her total annual revenue that decreases the amount of corporate income tax payable to the budget;

2. Exemption of the taxpayer from the property tax. This preference is granted only for the permanent assets once again placed in operation, which are on the balance and used in the framework of investment project;

3. Exemption from the land tax on the ground areas purchased and used for the realization of investment project.

The investment tax preferences may be granted for the period up to 5 years depending on the volume of investments.

We would like to draw your attention to the fact that investment tax preferences ARE NOT GRANTED:

1. If the special tax treatment is used with respect to the activity of your legal entity;
2. If your legal entity is the subsoil user on the basis of corresponding Contract concluded with the authorized body of the Republic of Kazakhstan;
3. With respect to the fixed assets of your legal entity if they were given in the form of state natural grants.

The exemption from customs duties

This type of preferences is granted for the import of equipment and its component parts assigned for the realization of investment project in accordance with Investment contract.

It is necessary to comply with the following conditions to get the exemption from customs duties for the imported equipment and its component parts (hereinafter "imported equipment"):

1. There is no production of imported equipment in the territory of Kazakhstan;
2. There is the production of imported equipment in the territory of Kazakhstan, but it is not sufficient to realize the investment project;
3. The equipment produced in the territory of Kazakhstan does not comply with the requirements made in the framework of investment project realization.

The exemption from customs duties is granted for 1 year with possible prolongation of this term. The maximum term of this type of preference is 5 years following the moment of Investment contract registration.

To get this investment preference the Investment Committee of the Ministry of Industry and Commerce of the Republic of Kazakhstan should send the notice about granting the exemption from customs duties for your legal entity to the Customs Supervision Agency of the Republic of Kazakhstan.

The notice should include the following information:

- name of investor;
- date and number of Investment contract;
- list of equipment and its component parts exempted from the customs duties;
- validity period of this preference.

After it the Customs Supervision Agency of the Republic of Kazakhstan will send this data to the customs authorities, which will carry out the customs registration and control of the imported equipment.

The state natural grants

The state natural grants are given by the Government of the Republic of Kazakhstan or by the Investment Committee of the Ministry of Industry and Commerce of the Republic of Kazakhstan. **The following may be transferred as state natural grants:**

- ground areas;
- buildings, constructions;
- machines and equipment, transport facilities (except passenger cars);
- computers, measuring and control devices and instruments, production and household equipment.

The provision of state natural grants to the property or to the land tenure is coordinated with state authorities in the area of public property and land resources management. The coordination of state natural grant provision is made within 15 (fifteen) workdays following the moment when the relevant request was made.

The legislation determines the limitations for the provision of state natural grants. The maximum amount of the natural grant is equal to not more than 30% of the volume of investments to the fixed assets of legal entity registered in accordance with the legislation of Kazakhstan. The estimation of the amount of state natural grant is made according to its market value.

The procedure of granting the investment preferences

The **Investment contract** is the principal document, which includes the detailed information on the preferences provided for your legal entity by the Government of the Republic of Kazakhstan.

To get the investment preferences your legal entity should apply with request to the Investment Committee. The following documents should be produced together with your request:

1. Notarized copy of Legal Entity State Registration Certificate;
2. Notarized copy of Legal Entity Statistical Card;
3. Notarized copy of the Charter of legal entity;
4. Business-plan of investment project which should be made in accordance with established requirements;

5. Documents that prove the budget of building and assembly jobs and charges for the acquisition of fixed assets used during the realization of investment project;

6. Documents that determine the sources and guarantees of project financing;

7. Documents that confirm the amount (cost) of the state natural grant requested by investor and preliminary coordination of its provision.

The Investment Committee examines this request within 30 workdays and, provided the compliance with the abovementioned conditions, makes a decision to grant the investment preferences. Then the Investment Committee prepares the Draft contract within 10 workdays and registers the Contract within 5 workdays following its signing.

The investment preferences terminate:

1. in connection with expiration of Contract;

2. in connection with anticipatory repudiation of Contract under the agreement of parties or on the initiative of one of the parties on the grounds provided in the Contract;

After the expiration of Contract your legal entity should start the payment of taxes and customs duties on general grounds provided by the existing legislation of the Republic of Kazakhstan.

In case of anticipatory repudiation of Contract your legal entity should pay the sums of taxes and customs duties and return the property received as natural grant, imposing a fine and using the punitive measures (in case of Contract repudiation on the initiative of the Investment Committee or investor) or without them (in case of Contract repudiation under the agreement of parties).

The law firm "GRATA" has a many years' experience of holding the negotiations for granting the Investment preferences and signing the Contract with the Investment Committee on terms which are the most acceptable for the investor.

General Provisions of the Law of the Republic of Kazakhstan "On Investments"

Investments are an important part of the state economics. The annual investments in capital estimated by the International Bank of reconstruction and development is $0,7-1,2 trillion, including $0,13-0,24 trillion of direct investments and $0,12-0,67 trillion of portfolio investments.

Since the moment of independence, the Republic of Kazakhstan actively takes part in international relations. Kazakhstan is the attractive object for foreign investments, and the main reason is rich natural resources. The state holds 13th place in the world due to it's natural resources: 2,2 billion tons of oil, 5,5 trillion cubic meter of the natural gas, and 0,7 billion tons of condensate. In regard to iron ore resources, Republic of Kazakhstan takes 11th place in the world.

During the period from 1994-1999, Kazakhstan has attracted investments in the amount of $7794,2 million. In 2001 investment dollars increased to $18 million, and in 2002 - more than to $20 million.

The public investment policy of the Republic of Kazakhstan is facilitated by consideration and ratification of laws and state programs.

The important event in the investment policy is an enactment of a Law "On Investments". The Law of the Republic of Kazakhstan "On Investments" (hereinafter "the Law") dated 08.01.2003 includes 4 Chapter, 23 articles and has a range of particularities:

1. The legislator does not use a term "foreign investments", consequently the Law has no definition of foreign and domestic investments;

2. The Law "On investments" has no definition of direct and indirect investments;

3. In accordance with provisions of the Law, investment preferences will be determined individually in each investment project. The duration of investment preferences should not exceed 5 years from the moment of coming into effect of the investment project.

4. To settle disputes in the court, it is necessary to have agreement of the parties (the State and the Investor) to determine the competent court, when the Law of the Republic of Kazakhstan "On foreign investments" dated 27.12.1994 granted such right to the investor.

5. Reduced the list of guarantees to investors within territory of Republic of Kazakhstan.

In essence, the Law "On Investments" dated 08.01.2003 formed from two legal parts: legal regime of investments, and state support of investments.

According to art. 1 of the Law, investments recognized as all types of assets (except goods designed for personal consumption), including subject of leasing from the date of conclusion of leasing contract, and rights to such assets invested by the investor to charter capital of the legal entity, or to increase in assets usable in business activity.

Investors have the right to invest in all objects and types of business activity with the exception of cases established by the current legislation of the Republic of Kazakhstan.

Investment guarantees

Investors have the following guarantees within the territory of the Republic of Kazakhstan:

1) The guarantee of legal defense of investors' activity within the territory of Republic of Kazakhstan;

2) The guarantee of using a revenue earned by the investor;

3) Publicity of activity of state authorities in respect to investors.

4) The guarantee of investors' rights in case of nationalization and requisition.

Investment preferences

The Law "On Investments" stipulates that the below investment preferences obtained by investors at the moment of concluding the Contract with the Competent state authority of the Republic of Kazakhstan (in present – the Investment Committee of the Republic of Kazakhstan):

1) investment tax preferences;

2) exemption from customs duties;

3) state grants in kinds.

Conditions to provide these investment preferences are the following:

1) concordance of specified investment activity to the list of priority types of activity alleged by the Government of the Republic of Kazakhstan;

2) investment of capital to fixed assets of the legal entity of the Republic of Kazakhstan to establish new production, extend and/or update operating enterprises by using higher technologies;

3) submitting necessary documents sustaining presence of finance, technical and managerial resources of the investor to realize investment project.

Application on receiving investment preferences should be submitted to the Competent authority of the Republic of Kazakhstan. The Competent state authority makes decision on providing investment preferences and notifies the investor on this, in writing within 30 days from the date of registration of the application.

In general, investment preferences remain in force till the validity term of the appropriate investment contract.

Conclusion and termination of the Investment contract

The Competent authority of the Republic of Kazakhstan prepares the Investment contract, on the basis of provisions of the Model contract, for signing within 10 days after making decision to provide by the investment preferences. The Investment contract becomes effective from the moment of it's state registration, which takes place within 5 days from the moment of signing the Contract by the parties.

In compliance with art. 22 of the Law "On Investments" the Investment contract may be terminated at any time upon:

1) under mutual agreement of the parties;

2) in one-sided order.

A basis to terminate the Investment contract, in one-sided order by the Republic of Kazakhstan, is falsification or suppression of information submitted by the applicant, and also non-performance it's obligations under the contract by the investor.

International regulation of the investment process also has positive influence on the state economics. For this purposes, the Republic of Kazakhstan has entered the international organisations, concluded bilateral and multilateral treaties directed to defence and stimulation of investments. Thus, on 6th of December 2001, the Republic of Kazakhstan passed the Law "About membership of the Republic of Kazakhstan in International Monetary Fund, International Bank of reconstruction and development, International Finance Corporation, International Development Association, Multilateral Agency on investment guarantees, International Centre of settlement of investment disputes, European Bank of reconstruction and development, Asian Bank of development, and the Islamic Bank of development" which regulates questions of membership in above organisations.

Features of Land Legislation of Republic of Kazakhstan with Regard to Subsoil Users

The subject of this present information for clients, is the practice of obtaining the land use rights by subsoil users. Please note that the new Law "On land" was adopted June 20 2003. Many subsoil users are interested in how it influenced upon the order of obtaining the land use right, or whether there are features of new land legislation pertinent to the subsoil users.

First, we would like to state that the new Law "On land" did not change severely the order of obtaining land use right by subsoil users. The most essential changes took place in the legal regulations of relationships concerning allotments of agricultural purpose.

Comprehension of the subsoil user right

Comprehension of the subsoil use right is considered a right of possession and subsoil right within the limits of Contract territory rendered to subsoil user, in accordance with the order established by legislation of Republic of Kazakhstan. Subsoil right provides to its owner, the power to execute the works related to geological research of subsoil, prospecting and mining, including the works connected with prospecting and mining of groundwater, medical filth, prospecting of the subsoil for fault of soil water, as well as the works for construction and exploitation of underground building not connected with the mining.

The owner of subsoil right is obliged to obtain the permission for use of their allotment on which they have plans to execute subsoil operations.

Order of obtaining the land use permission

Legislation provides the oblast executive body (city of republican purpose) – the Akim, decides the issue on submitting and requisition of allotments for purpose of subsoil use. The rendering of allotments for execution of activity related to the subsoil, is performed only after obtaining and registration of a subsoil right. At the same time, the subsoil contract is the basis for immediate legalization of allotments.

Legislation provides separately for the subsoil right for mining of generally used minerals for ones own necessities, to be transferred with land use right simultaneously.

Granting the right for use of state allotment to subsoil users is performed in following consecution:

1) abapplication to local executive body on submitting the land use right;

Subsoil users are obliged to join the copy of the subsoil contract to application. The application is considered during three months.

2) abpreparing and approving the project of organization for the use of land;

3) abdecision of oblast executive body (city of republican purpose), on submitting the land use right to subsoil user;

The decision on submitting of the allotment, or refusal of submitting the allotment, is adopted on the basis of the conclusion of a commission being made up by a local executive body from the members of local representative bodies, representatives of territory land resources authorities, architecture and town-planning bodies, and local self-government bodies.

4) abestablishment of the scope of allotment on-site;

5) abpreparation and issue the documents confirmed the right on an allotment;

The oblast executive body (city of republican purpose), decides on granting the land use right and is entrusted with preparing the lease agreement with owner of subsoil right, for term of validity of subsoil contract, with the Land resources authority (hereinafter referred to as "Land Committee").

6) state registration of the land use right.

If the **contract territory is in private property or belongs to private persons,** the local executive body, in case of need, is entitled to withdraw the allotments submitted, and submit other equal allotments instead.

Order of registration of land use right

On the basis of the decision of the local executive body (city of republican purpose), the Land Committee prepares the lease agreement with the local executive body (city of republican body), from one side, and owner of subsoil right, from another side. The registration is performed during the five working days from the moment of submission of the application by the owner of the subsoil right.

Lease payment for land use right

The amount of annual lease payment is established within the limits of 100%-120% of basis rate of payment for land use right, approved by Government of Republic of Kazakhstan:

The basic rate of payment for allotments in case of state rent or state land users rent, is equaled to the amount of the land tax calculated per allotment in accordance with tax legislation of Republic of Kazakhstan. The growth class number is taking into account in calculation land tax dependant on which the basic rate of payment is changed. The amount of lease payment is established calculated upon one hectare.

Order of restitution of the allotment to the state

The conditions and order of restitution of an allotment used for subsoil purposes, is determined by subsoil contract.

After termination of validity of subsoil contract, or on stepwise restitution of Contract territory, the Contractor shall transfer the contract territory in a state which is suitable for further use upon direct purpose in accordance with legislation of Republic of Kazakhstan. Any transgressions (deteriorations) against the environment within the contract territory during the validity of Contract, shall be restored at the expense of the Contractor, until matching the conditions suitable for further use for direct purpose. Until termination of validity of Contract, or at the latest of two years from the moment of beginning of validity of a mining contract, the subsoil user shall submit the program of liquidation of consequences of their activity according to the contract, to the Geology and Subsoil Protection Committee for approval, including the expenses estimation for liquidation. The liquidation program shall include the cancellation and liquidation of constructions and equipments used during the procedure of activity of Contractor upon the contract territory. For the complete financial provision of the execution of the liquidation program, the Contractor shall establish a liquidation fund. The Subsoil user is obliged to pay periodically to the liquidation fund, on deposit to an account in any banks of Republic of Kazakhstan. After liquidation of all consequences of execution of operations for subsoil purposes, the Geology and Subsoil Protection Committee shall decide on the transfer of the allotment to oblast executive body (city of republican purpose).

Thus, we would like to conclude that the new land legislation did not resolve the problems of subsoil users. We note that in accordance with the Land Code, the subsoil contract is the basis for immediate legalization of land use right upon the Contract territory. However, as practice shows, the procedure of consideration of an application of subsoil user, from submitting the land use right upon the Contract territory lasts approximately three months. That is why, we currently think that there is the requirement to elaborate the submission procedure for subsoil users.

Quoting Oil Export in Republic of Kazakhstan

First of all, we would like to draw your attention on the provisions of the current legislation, regulating the oil supplies in the home market of the Republic of Kazakhstan.

Accoiding to the current legislation, the State has the right to demand the oil requisition only in the following cases:

1. In accordance with Article 36 of the Decree "About Oil" (Requisition and compensation of the Oil) **in cases of war, natural disasters or other cases, provided by the legislation on emergency situations,** the Government of the Republic of Kazakhstan possesses the right to requisite the part or the whole amount of the oil, belonging to a subsoil user on the basis of proprietary right or right for economic management. The requisition is realized within the volumes, necessary for provision of needs of the Republic of Kazakhstan during the whole period of emergency situations.

   According to the Law of Kazakhstan Republic as of 05.07.96 "About emergency situations of natural and man-caused origin", an emergency situation is considered to be situation on a definite territory, **that has arisen in the result of accident, disaster or catastrophe,** which has entailed or can entail the deaths of people, damage to their health, damage to environment and the objects of economic activity, significant material losses and breach of the public living conditions.

2. According to p.l of Article 35 of the Decree "About Oil" (right of the Republic of Kazakhstan for Oil acquisition) "The Republic of Kazakhstan has the top priority for Oil acquisition from

the share of the subsoil user or non-governmental subsoil user at the prices of the world market. **The maximum volume of the acquired Oil, order of prices determination and type of payment are stipulated in the Contract".** Thus, the Contract for subsoil use (Oil Contract) should establish:

1) The volume of the oil, which the Government has the right to demand from the subsoil user in accordance with its right for priority acquisition;

2) Order of determination of world market price, at which the Government will acquire the oil from the subsoil user in a priority way.

3) Type of payment for oil acquired.

It is obvious, that the procedure of realization of the right by the government oh priority acquisition of the oil is deemed to be no less important matter, that should be the subject to negotiations between the State and the subsoil user during signing of the Oil Contract. But Oil contracts do not always regulate this procedure, in connection with this there exist a practice of unilateral regulation by the competent state authority - the Ministry of Energy and Mineral Resources of the Republic of Kazakhstan (MEMR)- of oil supplies to the home market and for export by the way of confirmation of the schedules for supplies of this kind.

For the present day, the situation with determination of the quota on oil supplies and export to **the Kazakhstan oil processing plants (OPP) is the following:**

In August 2000, Decree # 1172 of the Government of Kazakhstan Republic as of 02.08.00 "About some questions of stabilization of the oil products home market" (hereinafter "Decree") was adopted. According to the Decree, oil companies have guaranteed the definite volume of monthly oil supplies for Kazakhstan oil processing plants. At the same time the MEMR should have approved the schedules of this supplies till the end of year 2000. In other words, the Decree was of temporary nature – till the end of 2000.

In spite of the fact that the Decree hadn't any changes made, related to schedules confirmation for the year 2001, 2002 and 2003, for the present day the MEMR continues to approve the schedules of oil supplies for oil processing plants and oil companies. At the same time the quotas for oil export are also approved by the MEMR.

Beginning from July 1, 2003 the Law of the Republic of Kazakhstan "About Changes in statutory acts of the Republic of Kazakhstan, concerning the issues of state regulation of production and turnover of separate kinds of oil products" (hereinafter "The Law") has become effective and made the following amendments in the Decree "About Oil":

- in Article 5 of the Decree "About Oil" the competency of the Government of the Republic of Kazakhstan has been amended with the following authorities.

  The Government of the Republic of Kazakhstan:

  1) Regulates the oil export, including by the way of approval (changing) of excise-duty rates, customs, protective, anti-dumping and compensatory duties, as well as quotas on oil export.

  2) Establishes the quantitative restrictions (quotas) for oil transportation by various kinds of vehicle.

  3) Determines the order of oil production and turnover unified database maintenance.

  4) Organizes the system of control over the observance of safety requirements in the technological process of oil production, storage and turnover.

- in point 1 of Article 6 the functions of the competent authority have been enlarged:

The competent authority accomplishes state regulation of oil production in accordance with the project for field development, as well as for its turnover.

It is possible to suppose, that as the consequence of the Law coming into force, there will be adopted a respective Decree of the Government for regulation of the quotas issue for oil export. It means that the actions of the MEMR on regulation of oil supplies to the home market and for export will have an official legal character.

It is not excluded that due to the Decree of the Government, this or any other subsoil user will be refused to give a quota or the authorized quota will be less than the oil volumes, applied for export by the subsoil users to the competent authorities. In this case the Decree can be acknowledged as the violation of Article 71 of the Law "About subsoil and land resources use": changes and amendments of the legislation, aggravating the position of the subsoil user, are not applied to the Contracts, issued or concluded before such changes or amendments.

The authorities of the Government for determination of the quotas for oil export and transportation, set by the Law, are not the aggravation of the subsoil user position, therefore are applied to the Oil Contacts. But, if the related Decree of the Government will establish for the, subsoil user an export quota, less than provided by the Oil Contract, the subsoil user reserves the right for protection of his interests judicially.

On the given matter the main subject of the negotiations of subsoil users with the competent authority will be the volumes of oil supplies for the Kazakhstan oil processing plants and prices for oil acquisition at hone market.

The disputable situation can arise, if the actual volumes of the produced oil will differ from the volumes, set by the work program of the subsoil users for the corresponding year (exceeding or less volume):

- there will be the necessity to review the oil export volumes and volumes of supplies for the Kazakhstan oil processing plants. One of the decisions, taking into consideration the interests of both subsoil user and the Government, is the proportional increase (or decrease) of export quota or volume of supplies for the Kazakhstan oil processing plants.
- if in the result of the production volume increase, the prices on oil will also increase, there will be the necessity to review the price on oil sale to Kazakhstan oil processing plant. In this case the question can be solved in the following way – oil will be sold according to the earlier agreed prices, provided that the oil will be supplied in volumes agreed upon earlier.

Also beginning from July 1, 2003, the Law "About state regulation of the production and turnovers of the separate types of oil products" has become effective.

This Law regulates the production and turnover of the petroleum (excluding aircraft motor gasoline) diesel oil and fuel oil, and in general contains the *restrictions for oil products manufacturers* - oil and (or) gas-processing enterprises, having the license to production and sale of oil products in accordance with the legislation of the Republic of Kazakhstan.

For the suppliers of oil - oil-gas producing enterprises, that supply for processing their own crude oil and (or) gas condensate, the indicated Law establishes the following requirements and obligations:

- Sale of gasoline (excluding aircraft motor gasoline) diesel oil and fuel oil is admitted via measuring devices of the oil products manufacturers, and also from filling stations and oil products storehouses, the services of which are certified.
- Submission to the authorized organs the information to carry out monitoring;
- Execution of the accompanying waybills during wholesales and retail sale of oil by the suppliers and at realization of oil products transportation operations.

The Law doesn't include the innovations relating to regulation of export and import of oil products, it contains only the references to the current legislation.

Thereby:

The approval of the quotas on oil export and schedules of oil supplies to Kazakhstan oil-processing plants is not governed by the current legislation. Determination of quotas for oil export and supplies to Kazakhstan oil processing plants is the imperative requirements of Ministry of Energy and Mineral Resources, and at the same time the given requirements are ungrounded and can be acknowledged as illegitimate judicially. The absence of the precedent on the given matter can be explained as the unwillingness of the subsoil users to apply for protection of their rights to the judicial authorities, as it can negatively effect on their mutual relations with competent authorities.

Procedures of Obligatory Tenders Holding in the Course of the Purchase in the Oil and Gas Branch

All issues connected with the above mentioned procedure shall be settled by the Rules of goods, works and services procurement during the oil operations adopted by the Order as of June 7, 2002 of the Government of the Republic of Kazakhstan.

In accordance with these Rules, the procurement of goods, works and services by enterprises of oil and gas branch, shall be carried out on the basis of tender.

The above Rules shall determine the methods and terms of goods, works and services procurement during the performance of oil operations.

General provisions of these Rules:

1) The Ministry of Industry and Commerce of the Republic of Kazakhstan was determined as the authorized state body responsible for regulation of goods, works and services procurement during the oil operations performance.

The authorized state body shall control the goods, works and services procurement during the oil operations performance and also it approves the results of the tender for the goods, works and services procurement during the oil operations performance.

2) The new methods for carrying out of the procurements were determined. Therefore the tender (of open and closed type) is provided and the procurement without tender is permitted.

3) The requirements were established for the procurement procedures.

The essential moments of the procurement procedures are consisted in the following:

1) The authorized body of the subsoil user established the requirements for decision making about the procurements carrying out.

2) The procedure for obtaining of the tender terms obligatory approval by the Subsoil user in the Ministry of Industry and Commerce of the Republic of Kazakhstan was established the above terms include:

the information about the tender shall be addressed to the potential tender participators;

the tender documentation;

the provision of the tender commission.

3) The Protocol made according to the tender results, shall also subject to the approval in the Ministry of Industry and Commerce of the Republic of Kazakhstan.

4) The Ministry of Industry and Commerce of the Republic of Kazakhstan representative shall be obligatory included to the tender commission.

5) "Tender Organiser" institution shall be provided. I. e., the Subsoil user may charge any third person with the co-ordination, organization and carrying out of the procurements in accordance with the above Rules.

In case of the procurements carrying out without tender, it is also necessary to obtain the permission of the Ministry of Industry and Commerce of the Republic of Kazakhstan.

Order of the tender holding

After the approval of the Tender Terms, the tender Organiser informs the potential participators about holding of the tender. The tender information shall be addressed to the potential tender participators not later than 30 days prior to bids receiving deadline.

The method of potential participators notification shall correspond with the form of the held tender. During the open tender holding, the information about such tender shall subject to publication in the periodicals of the Republic of Kazakhstan.

During the tender holding, the Kazakhstani enterprises manufacturing the goods, performing the works, rendering the services and which corresponds with the tender terms, standards and the other requirements made to the oil operations, shall be attracted in the priority order for participation in the tender.

Holding of the tender, exclusively among the foreign organizations, if the Kazakhstani enterprises manufacturing the goods, performing the works and rendering the services in the territory of the Republic of Kazakhstan exist, and which correspond with the tender terms, standards and the other requirements to the oil operations, shall be forbidden by the Rules.

Main Provisions of the Law of the Republic of Kazakhstan "About State Control When Applying Transfer Prices"

On January 5, 2001 The President of the Republic of Kazakhstan signed the Law of the Republic of Kazakhstan "About State Control When Applying Transfer Prices" (hereinafter referred "the Law"). This Law establishes basic regulations for realization of state control when applying transfer prices and also the provisions for rating the prices applied as transfer prices.

1. Transfer price

What does it mean – transfer price? In accordance with article 2 of the Law transfer price is "a price that differs from the evenly formed market price applied when conducting transactions established by the Law". Thus the notion "transfer price" is formed from two key criteria:

1) the price being applied by the parties shall differ from the evenly formed market price;

2) a transaction the price of which differs from the market price shall come within the parameters described in the Law itself.

2. The order and methods of the market price determination

From the information mentioned above a question can emerge: how can we determine the evenly

formed market price? Article 7 of the Law establishes the following methods:

1. the method of the comparable uncontrolled price;

2. "expenses plus" method;

3. the method of subsequent realization.

The method of the comparable uncontrolled price is applied in the presence of transactions on identical (in case of their absence – similar) goods at the appropriate market of goods, works and services (hereinafter – goods) and this method establishes a market price from the prices for identical (in case of their absence – similar) goods sold under the comparable conditions to a purchaser not related with the vendor.

The "expenses plus" method is a method when the market price of goods is determined as a sum of expenses and extra charges. In this case all confirmable direct and indirect expenses for production (purchasing) and (or) realization of goods, transport charges, storage costs, insurance and other expenses shall be taken into account. Extra charges are established in such a way that it could provide average level of economic efficiency appropriate to the given scope of activity.

The method of subsequent realization is a method when the market price is determined as difference between the price at which the goods were realized by the purchaser after subsequent realization and confirmable expenses taken by the purchaser at on-selling without taking into account the price at which the goods were bought by the purchaser and his extra charge. Extra charges are established in such a way that it could provide average level of economic efficiency appropriate to the given scope of activity.

The "expenses plus" method and method of subsequent realization are applied in the absence of transactions on identical (in case of their absence – similar) goods at the appropriate market of goods, works and services and also in the case of impossibility to determine the appropriate prices failing information sources or their unaccessibility.

Apart from the determination of the market price the Law provides the opportunity of taking into account the conditions affecting the diiference between the price market and the price being applied. Such conditions are the following:

1. quantity (volume) of the goods being supplied (for example the consignment volume), количество (объем) поставляемых товаров (например, объем товарной партии), the works being performed and the services being rendered;

2. quality of goods being supplied or purchased, availability or absence of packaging and easy-to-use prepacking;

3. terms of obligation performance;

4. payment terms and conditions usually being used in transactions of the given type and other conditions that can affect the prices;

5. usual discounts and extra charges to the prices in transactions between non-interrelated persons. In particular discounts and extra charges made under the following conditions are taken into account:

! seasonal variations in customer demand for goods (works, services);

! loss of quality of goods or other consumer characteristics;

! partial improvement or repair of lost quality or other consumer caracteristics of goods;

! expiration (forthcoming expiration) of the use-by date or realization date of the goods;

! marketing policy when forwarding new goods (works, services) having not any analogues at the market and also when forwarding goods (works and services) to new markets;

! realization of test patterns and models of goods with the purpose of their representation for consumers.

The difference between the price being applied and the market price is not a reason for correction of taxation objects.

According to article 9 of the Law any information sources may be used for determination of the market price of goods, including:

1. sources of information about market prices for goods;

2. officially recognized resources of information about exchange quotations;

3. the information being submitted by the participants of transactions to the authorized bodies.

The list of the official sources of information on market prices is determined by Goverment Regulation of the Republic of Kazakhstan No. 788 as of 09.06.2001 "About approval of the list of official information sources concerning market prices for specific types of goods subject to state control at application of transfer prices in international transactions". In accordance with this list the following information sources are acknowledged as official:

- Petroleum Argus (Oil export and Neftepanorama editions);
- News agency "Reuters" (Energy 2000 and Commodities 2000 editions);
- Metal Bulletin Journals Ltd. ("Metal Bulletin" journal);
- The McGraw-Hill Companies (Platt,s Crude Oil Marketwire H Platt,s European Marketscan), and also other sources stated in the mentioned Regulation.

In other words, any information about prices, discounts, extra charges etc. obtained from the stated sources of information is acknowledged as official and mandatory for state authorities of the Republic of Kazakhstan and may substantially affect the state control application to one or another transaction using transfer prices.

3. The transactions coining within the state control if the transfer prices are applied

According to article 3 of the Law the state control for discovering the cases of transfer prices application is exercised on the following types of transactions:

1. between interrelated or interconnected parties;
2. on barter transactions;
3. when fulfilling obligations for transactions being performed by means of taking into account a similar counter claim (including set-off for cession);
4. at settlement of the transactions with the persons registered (residing) in foregn countries or having accounts in foreign banks whose legislation does not provide a possibility of disclosure and submission of the information about financial transactions or if preferential tax treatment is applied in the locality of their registration (residing) including offshore areas;
5. at settlement of the transactions with the juridical persons having tax priviliges or for which another taxation rate is set that differs from the rate set by tax legislation.
6. at settlement of the transactions with the juridical persons having losses according to the information given in tax statements during the last two tax periods previous the year of settlement of the transaction;
7. when performing international business operations (i.e. with participation of non-residents of the Republic of Kazakhstan) in the case of discovering the fact of difference between the transaction price and market price of more than 10% in both directions from the market price.

Thus the Law establishes seven conditions (types of transactions) to which the state control may be applied if transfer prices are used. If only one condition from mentioned above is present, it is enough for application of such control.

4. The consequences of exercising the state control in the case of transfer prices application

According sub-section 5 of article 5 of the Law if the fact of difference between the market price and transaction price (i.e. if the fact of transfer price application is discovered) the authrised bodies correct the objects of taxation. I.e. in this case additional charging of income-tax, VAT, excise, royalty, excess profit tax, customs fees is performed and such additional charging is calculated in such a way as if the incomes and expenses from these transactions and other taxation objects would be determined upon the basis of the market price. Additionally penalties and fines are imposed.

Certification of Equipment in the Republic of Kazakhstan

This information will be useful for the companies importing equipment to the Republic of Kazakhstan including the equipment for oil -and- gas industry.

The Basis of Certification

Certification of the equipment in the Republic of Kazakhstan is regulated by the following principal standard legal acts of the Republic of Kazakhstan:

1. The Law of the Republic of Kazakhstan "On Certification", dated July 16 1999 #434-1;
2. The regulation of the Government of the Republic of Kazakhstan dated November 29, 2000 #1787 "On the Control of Products Conformity in the Republic of Kazakhstan";
3. "List of Products and Services subject to compulsory Certification" ratified by the regulation

of the Government of the Republic of Kazakhstan dated November 29, 2000 #1787;

4. State Standard of the Republic of Kazakhstan ST RK 3.4 - 94 (publication);

5. State Standard of the Republic of Kazakhstan ST RK 3.9 - 97 (publication);

6. "Instruction on the order of allowance for acceptance tests, granting of permission for production (serial) output and utilization of new domestic and foreign excessive danger products used in the branches of industry supervised by the state control authorities for prevention and elimination of the emergencies" ratified by the order of the Emergency Agency Chairman dated November 29 1999 #256.

The certification is necessary for the following purposes:

1) Provision of operational safety of the equipment for the life and health of the people, the property and environment;

2) Provision of technical and information compatibility;

3) Provision of safety for the economic objects, taking into consideration the natural and man-caused disasters risks;

4) Consumerism activity concerning the quality of products, (works) processes and services;

5) Arrangement of conditions for the activity of natural and legal persons on the goods market of the Republic of Kazakhstan and for participation in the international economic, scientific and technical collaboration and in the international trade.

Types of certification

The legislation of the Republic of Kazakhstan provides for obligatory and voluntary certification.

The Subject to the obligatory certification is the equipment specified in the list of goods, works and services ratified by the Government of the Republic of Kazakhstan.

The Accredited certification bodies can provide certification on request of the Applicant (manufacturer, vendor, executive) (voluntary certification).

The Legislation of the Republic of Kazakhstan prohibits advertising and utilization of the equipment subject to certification in the Republic of Kazakhstan without certificates of conformity. Selling of the products subject to obligatory certification without certificates is also prohibited.

The Equipment subject to the obligatory certification

The following equipment subjects to the obligatory certification:

1. Agricultural machinery and equipment;

2. Electrotechnical, radio engineering and electronic equipment;

3. Heating equipment powered by oil, solid and gas fuel;

4. Woodworking equipment;

5. Building materials and constructions;

6. Light industry equipment;

7. Medical and veterinary facilities, medical and veterinary goods and sanitary means;

8. Fuel raw material resources;

9. Equipment for the potentially dangerous (hazardous) industries.

However one of the indispensable conditions for obtaining of **the State Control Authorities on prevention and elimination of emergencies Permission** for application of the foreign and domestic equipment in the Republic of Kazakhstan is providing of the **conformity certificate,** issued by the accredited certification center. Accordingly there is a list of the equipment subject to additional obligatory certification:

1. The Equipment for metal mining and coal industries, quarry equipment, grinding-sorting and agglomeration concentrating factory machinery;

2. The Equipment used in oil -and- gas producing industry, geological survey and main oil and gas products lines;

3. Chemical, petrochemical and oil-and-gas refining industries equipment;

4. The Equipment for metallurgy industry;

5. The Equipment used at the objects of boiler-gas facilities, lifting gear and bakery plants;

6. Equipment (processes) used for blasting operations;

7. Mine-and-gas rescue equipment, flow head protection equipment, technique and inventory, breathing apparatus, control instrumentation and recovery aids etc.

Certification Authorities

The authorized certification bodies in the Republic of Kazakhstan are the following:

1. The Authorized organization on standardization, metrology and certification (Standardization, Metrology and Certification Committee under the Ministry of Industry and Commerce of the Republic of Kazakhstan);
2. Accredited bodies on certification of products, processes, works and services;
3. Accredited testing laboratories (centers);
4. Accredited organizations on rendering of consulting services in the area of accreditation;
5. Experts-auditors in certification.

Marking of the equipment with the compliance mark is performed by the manufacturer by the methods providing the sharp image, resistance to the external influences, durability and etc. The certification authority shall determine the Method and place of tagging.

Certification of the Imported Equipment

Certification of the equipment imported to the Republic of Kazakhstan shall be carried out in accordance with the same schemes and regulations established by the GSS of the Republic of Kazakhstan as those for the domestic equipment, providing for the observance of the payment equivalence principles for certification.

Decisions on the foreign certificates recognition are made by the authorized state body (Standardization, Metrology and Certification Committee under the Ministry of Industry and Commerce of the Republic of Kazakhstan). The documents for recognition are issued in the language of the importing country, Russian and Kazakh.

The following procedures for certification of the imported equipment are established in the GSS of the Republic of Kazakhstan:

- Acceptance of the certificates of conformance issued by the certification authorities of CIS countries, being the parties to the Agreement;
- Acceptance of the foreign certificates of conformance issued by the foreign certification authorities accredited in the GSS of the Republic of Kazakhstan;
- Acceptance of the copies of the certificate of conformance issued by the certification authorities of CIS countries, being the parties to the Agreement, attested by the certification authorities or enterprises, holding the certificate of conformity;
- Certification of equipment according to the requirements of ST RK 3.4.

Settlement of Tax Disputes

A tax audit frequently causes a lot of questions and indignation as to the inspection rules and results. In this connection we are glad to bring to your notice the information, which may prove useful for you in the nearest future.

1. What should you know about the tax audit

According to the legislation of the Republic of Kazakhstan the notion “tax audit” is an audit carried out by tax authorities to check, whether the tax legislation of the Republic of Kazakhstan is complied with or not. The audit may be carried out exclusively by the taxation authorities, such as:

1) Tax Committee of the RK Finance Ministry;
2) Oblast Tax Committees;
3) Regional Tax Committees;
4) Municipal Tax Committees;
5) District Tax Committees in cities.

Other public authorities of the Republic of Kazakhstan are not entitled to conduct audits as to whether the tax legislation is complied with or not.

Documented audits are the audit type taxpayers more frequently encounter.

To protect entrepreneurs from the permanent interference on the part of tax authorities the legislation of the Republic of Kazakhstan establishes an audits frequency. Overall audits are conducted not often than once a year; subject ones-not often than once in six months for the same tax type and other compulsory payment due to the budget. These restrictions are not applied to the following cases:

1. When the documented audits are conducted in connection with the reorganization and liquidation of legal person;

2. When the documented audits are conducted in connection with the expiry of the Subsoil Usage Contract validity;

3. When counter-audits are conducted;

4. When the subject audits are conducted based on the taxpayer's statement as to whether amounts of the value added tax claimed for recovery is reliable or not;

5. When additional audits are conducted based on the decision of the authority considering the taxpayer's complaint about the Tax Audit Report Notification;

6. When extraordinary audits are conducted pursuant to the authorized public authority head's order in respect of the particular taxpayer.

If none of the listed cases is applicable to your Company, the audits are to be conducted in accordance with the frequency established.

2. Commencement of the tax audit

Any audit carried out by the public authorities starts at the time, when an order is delivered. Auditors upon arrival at your Company to conduct the tax audit are bound to acquaint you with the Audit Assignment Order, which has to include the following:

1) Date and number of the Order Registration at the tax authority;

2) Name of the tax authority, which issued the Order;

3) Full name of the taxpayer;

4) Taxpayer's Registration Number;

5) Audit type;

6) Positions and full name of the auditors and other persons attracted to conduct the audit;

7) Audit period;

8) Tax period subject to the audit, when the documented audits are conducted.

Apart from the details listed in the Order, the stamp of the local prosecutor office body confirming the audit registration is to be affixed thereupon.

Even if one of the listed details is not available, you are entitled not to allow the auditors to conduct the audit, by reason of improper execution of the Audit Assignment Order.

If the Order is duly executed and a service certificate has been presented to you, you are bound to allow the auditors to enter a territory or premise to conduct the audit.

3. Tax audit

The tax audit period specified in the order should not exceed thirty business days after delivery of the order. However, the legislation provides for exceptions to this rule:

1) Audit period, when transfer prices are applied to, may be up to 180 days;

2) Audit period, when the legal person having a structural unit is audited, may be up to 60 days;

3) When the matters of special complexity are audited, the audit period may be extended by the superior tax authority for the period between 50 and 80 days, depending on whether the taxpayer has the structural unit or not.

Extension of the tax audit periods should be without fail documented by execution, registration and delivery of the additional order specifying the period for that the tax audit has been extended.

The tax audit period may be suspended for the following periods of time:

1) Between the times, when the tax authority request to submit documents has been delivered to the taxpayer and the documents so requested have been submitted by the taxpayer;

2) Between the times, when the requests have been sent by the auditors and the data and documents concerning such requests have been received.

During the audit you are bound to ensure, that the auditor has an access to all the documents relating to the audit subject and allow him/her to enter the sites connected with taxation for examination. You should take into account, that the tax audit should not suspend the taxpayer's activity or adversely affect the business activity results. If the auditor's actions result in negative consequences for our Company, you should immediately apply to a lawyer and analyze the auditors' activities lawfulness.

The auditors are entitled to seize the documents, constituting an offense. Seizure of the documents is carried out by officials with two witnesses being present. Seizure of the documents should be documented as a Minutes of Seizure, a copy of which is issued to the taxpayer. The Minutes of the documents and things seizure (Administrative Offense Record) should contain information of the seized documents type and details. The Minutes is signed by the auditor, who has executed it, the taxpayer, from whom the appropriate docu-

ments and things have been seized and witnesses. In case of refusal to sign the Minutes, there should be an appropriate record therein. After the case is considered in accordance with the decision adopted, the seized documents are returned or confiscated.

4. Completion of the tax audit

Upon completion of the tax audit the auditor executes the Tax Audit Report, which should without fail specify the following:

1) Place of the tax audit and date of the Report;

2) Audit type;

3) Taxpayer's full name;

4) Taxpayer's location, banking details and registration numbers;

5) Full name of the taxpayer's head and officials responsible for tax accounts and accounting and tax payments;

6) Data of the previous audit;

7) Audited period and general data of the documents submitted by the taxpayer;

8) Detailed description of the tax offense with a reference to the appropriate norm of the tax legislation being made;

9) Tax audit results.

The audit is considered completed upon delivery of the Tax Audit Report to the taxpayer.

Further the tax authorities based on the results reflected in the Tax Audit Report issue a Notification of the charged tax amounts and other compulsory payments to the budget, fines and penalties and send it to the taxpayer. If in the course of audit there appeared no violations of the tax legislation, the Notification on the audit results is not issued.

The Notification is the final decision of the tax authority based on the results of tax audit. The Notification must be executed in writing and contain the following details and information:

1) Notification and tax audit report registration date and number;

2) Taxpayer's full name;

3) Taxpayer's registration number;

4) Amount of charged taxes and other compulsory payments to budget, penalties and fines;

5) Essential elements of appropriate taxes and other compulsory payments to budget, penalties and fines;

6) Period and time of appeal.

The Notification must be fulfilled or appealed within 10 workdays as from the receipt. By results of the audit the following issues shall be solved as well:

1. On imposition of administrative discipline upon a taxpayer under the grounds provided for by Administrative Offence Code;

2. On transfer of tax audit materials to financial police authorities for a decision to be made on institution of proceedings.

The administrative discipline shall be imposed by way of a fine in case of a taxpayer failing to pay amounts of taxes and other compulsory payments to budget. In case of finding of violations the tax authority shall prepare a report and pass a Resolution on imposition of administrative discipline. These actions shall be performed if offence was committed after January 30, 2001. Tax authorities shall send tax audit materials to financial police authorities if the amount of unpaid taxes is 2000 monthly design rates or above.

We draw your attention to the matter that when signing each document submitted to you during audit period and after its completion it is necessary to indicate full name and title of the signatory.

5. Appeal of tax audit results

Tax Code of the Republic of Kazakhstan entitles a taxpayer to appeal tax audit results in accordance with the established procedure.

Upon completion of tax audit the tax authorities shall present a Notification of the charged amount of taxes to a taxpayer. This document may be fully or partially contested with a higher tax authority or court.

For the avoidance of unreasonable legal costs we recommend to primarily address your complaint to tax authorities.

Appeal of tax audit results with tax authorities

As said above, in case of finding of facts of failure to pay taxes the tax authorities shall serve to a taxpayer a Notification of the charged amount of taxes and other compulsory payments to budget (hereinafter "Notification").

Period for appeal to a higher tax authority is 10 (ten) workdays. Failure to comply with this requirement shall result in refuse to consider the appeal.

The following must be annexed to an appeal:

3. Audit Assignment Order;

4. Tax Audit Report;

5. Notification;

6. Documents confirming arguments set forth in the appeal;

7. A document confirming powers of a signatory to the appeal.

When addressing an appeal to a higher tax authority a copy of appeal shall obligatorily be sent to the tax authority, which conducted the audit. It is necessary for the following:

1. Filing of an appeal for Notification shall suspend its execution. That is, the lower tax authority shall not have the right to arrest your bank accounts and recover the charged amount of taxes until a decision is made on the appeal;

2. Appeal by a taxpayer of tax audit results with higher tax authorities shall suspend transfer of materials to financial police authorities until an appropriate decision is made by a higher tax authority.

As you can see, by sending an appeal to a higher tax authority and a copy to the auditing tax authority you will make yourself secure against arrest of bank accounts and intervention by financial police authorities.

A higher tax authority is obliged to consider your appeal within 30 workdays. For especially complicated tax issues the period for appeal consideration may be extended. Tax authorities may demand to submit additional documents or call for explanations on arising issues.

After considering an appeal a tax authority shall make one of the following decisions:

1. to leave the appealed Notification unchanged, and appeal unsatisfied;

2. to revoke the appealed Notification in full or in part;

3. to send an order to a lower tax committee to conduct additional audit on differences.

In case your appeal is left unsatisfied you will retain a right to address your appeal to the Tax Committee of the Ministry of Finance of the Republic of Kazakhstan. We request you to note the following. When tax audit is conducted by the Tax Committee of the Ministry of Finance appeal shall be filed with the same tax committee, and its decision on appeal may be further appealed only with judicial authorities.

Term for addressing an appeal to the Tax Committee of the Ministry of Finance shall be 5 (five) workdays. Delay in appealing within this period shall result in refuse to consider an appeal.

The following must be annexed to an appeal:

1. Audit Assignment Order;

2. Tax Audit Report;

3. Notification;

4. A copy of appeal addressed to a lower tax committee;

5. Response to appeal from lower tax committee;

6. Documents confirming arguments set forth in the appeal;

7. A document confirming powers of a signatory to the appeal.

The Tax Committee of the Ministry of Finance shall consider an appeal within 15 (fifteen) workdays and shall make one of the following decisions:

1. to leave the appealed Notification unchanged, and the appeal unsatisfied;"

4. to revoke the appealed Notification in full or in part;

5. to send an order to a lower tax committee to conduct additional audit on differences.

In case your appeal is unsatisfied you may refer to judicial authorities requesting to annul the Notification and decisions of tax authorities in full or in part.

Judicial consideration of taxpayer's appeal

Legislation of the Republic of Kazakhstan establishes a five-year term for appeal of tax audit results judicially. However, we recommend to refer to the court prior to expiry of ten working days as from making a decision on appeal by a tax authority. Otherwise tax authorities may arrest your accounts and recover the charged amount of taxes and other compulsory payments.

To initiate a judicial procedure by location of auditing tax authority a statement of claim is filed.

The following must be annexed to a statement of claim:

1. Copy of statement of claim for appellee (tax authority);
2. Audit Assignment Order;
3. Tax Audit Report;
4. Notification;
5. Copy of appeal addressed to a lower tax committee;
6. Response to appeal from lower tax committee;
7. Documents confirming arguments set forth in the appeal;
8. A document confirming powers of a signatory to the appeal;
9. A document confirming the payment of state duty at the rate of 1 (one) per cent of the appealed amount. The appealed amount shall also include fines (imposed for a period until January 30, 2001) and penalties.

The court shall consider taxpayer's statement of claim within two months as from the receipt of statement.

By results of case consideration the Court shall pass one of the following judgments:

1. to leave the appealed Notification (decision of tax authority on appeal) unchanged, and statement of claim unsatisfied;
2. to declare the appealed Notification (decision of tax authority on appeal) illegal in full or in part.

This judgment may be appealed by a taxpayer, tax authority or attorney by appeal proceedings.

We request you to note that in accordance with internal deeds tax authorities are obliged to appeal each decision made not in favor of them to the last decree of jurisdiction. Due to this judicial consideration of tax disputes takes a lot of time and requires significant efforts from a taxpayer.

Appeal of a resolution imposing administrative discipline

We already mentioned administrative discipline imposed in case of improper fulfillment of tax obligations.

Before adoption of the new Administrative Offence Code (Administrative Code) on January 30, 2003 fines for untimely and incomplete discharge of taxes and other compulsory payments to budget were charged under a Notification. After giving effect to Administrative Code fines started to be charged under a separate Resolution.

This resolution may be appealed with a higher tax authority or court.

Term for appeal of the Resolution is 10 calendar days. Please note that calendar days are used for dating of period.

The Procedure of Recognition and Enforcement of International Arbitration Courts Decisions in the Republic of Kazakhstan

Many companies, which implement their activities in the Republic of Kazakhstan, provide for in contracts that disputes will be settled by international arbitration court.

All international arbitration courts decisions concerning the interests of Kazakhstan legal entities must be recognized and enforced in the Republic of Kazakhstan.

Considering that the Existing Legislation of the Republic of Kazakhstan, regulating the proceeding for recognition and enforcement of international arbitration courts decisions, has considerable gaps and it is quite intricate, companies face to certain difficulties.

The state authority, responsible for recognition and execution of decisions of international arbitration courts in the Republic of Kazakhstan

As a result of careful analysis of the existing legislation norms of the Republic of Kazakhstan and international legal acts, and studying of practice of application of this norms, we would like to inform that the following state authorities will be involved in the procedure for recognition and enforcement of international arbitration courts decisions:

- The Ministry of Justice of the Republic of Kazakhstan;
- Justice agencies of international countries;

- The Ministry of Foreign Affairs of the Republic of Kazakhstan;
- Embassies and Consular Offices of the Republic of Kazakhstan located abroad; Embassies and Consular Offices of foreign countries in the Republic of Kazakhstan;
- The Supreme Court of the Republic of Kazakhstan;
- Court Administration Committee attached to the Supreme Court of the Republic of Kazakhstan (hereinafter referred to as a "Committee");
- Territorial subdivisions of the Committee;
- Local courts of the Republic of Kazakhstan.

The mam state authority of the Republic of Kazakhstan, which is responsible for enforcement of decisions of international arbitration courts in the Republic of Kazakhstan, is Committee. However, the procedure of preparation and submission of documents to the Committee can be presented in **three following variants:**

I – Variant: the documents are to be certified by the state institution authorized to confirm legal force of the documents. Then the documents are to be submitted to the Ministry of Justice of the Republic of Kazakhstan. After the consideration the documents are to be sent to the Committee, which determines and sends the documents to relevant local court at the defendant's place of registration. This court writes out executive document and sends it back to the Committee.

II – Variant: the arbitration court sends the documents to the Ministry of Foreign Affairs of the Republic of Kazakhstan, or to Consular Office of the relevant country in the Republic of Kazakhstan, one of them sends the documents to the Committee.

The Committee sends the documents to the relevant local court according to the defendant's place of registration, which writes out executive document and sends it back to the Committee for execution.

III – Variant: The documents are to be submitted to the Committee. The Committee verifies validity of international arbitration court decision and sends the documents to the local court according to the defendant's place of registration. The court considers the possibility of recognition of international arbitration court decision and issue of executive document.

During the recognition and enforcement of international arbitration court decision the Committee sends the documents to the territorial subdivision of the Committee.

The documents required for the recognition and enforcement of international arbitration court decision

According to Part 1 of Article 4 of the New York Convention as of 1958 "For declaring and carrying into execution international arbitration courts decisions" (hereinafter referred to as "The New York Convention"), for recognition of legal force and carrying into enforcement of international arbitration court decision in the territory of participating country, it is necessary to provide the following documents:

1. Properly certified original decision of international arbitration court, or properly certified copy of such decision;
2. Original agreement, according to which the participants of legal relationships will be obliged to submit to arbitration court all, or any disputes, arising from, or which can arise between the participants, and the object of which can be subject of arbitration, or properly certified copy of such agreement.

Also local court, which considers statement for declaration and execution of international arbitration court decision, will be entitled to request additional documents, which, for example, verify that:

- The defendant was properly notified of the ongoing consideration of the dispute in the international arbitration court, of arbiters appointment;
- International arbitration court decision is valid; etc.

Document of execution of international arbitration courts decisions

You should take into consideration that the Legislation of the Republic of Kazakhstan does not clarify what document is to be issued during enforcement of international arbitration court decisions in the Republic of Kazakhstan: either Order of court or Executive sheet.

Decision of the question concerning the executive document does matter, particularly for determination of the size of the government duty to be paid when applying to the court of the Republic of Kazakhstan.

Taking into consideration contradictory character of the Legislation, we recommend to use the practice of courts of the Republic of Kazakhstan and specialists' successful experience.

Currency Transactions Registration

On July 25, 2003 the National Bank of the Republic of Kazakhstan adopted the new **Rules for licensing of the transactions connected with the usage of the currency values** and the **Rules for registration of the currency transactions connected with the capital flow and opening of accounts abroad** (July 4, 2003).

The new Rules adoption is connected with the changes in the legislative acts on the currency regulation made in spring of the current year and aiming at the liberalization of the currency regime in the territory of RK.

1. Currency Transactions Licensing

The following types of the currency transactions are the subject to licensing:

1) retail sale and services performance for the cash foreign currency;

2) opening *of the accounts with the foreign banks* by the residents;

3) residents' investments to abroad;

4) residents' remittances in favour of nonresidents for transactions providing the. transfer of the *property rights for the real estate* payment;

5) residents' remittances in favour of nonresidents for payments on the import transactions providing the advance payment for the goods (works, services) for the period exceeding 180 days and excess of the period of the currency receipt in return for the goods (works, services) export by the residents proceeds for more than 180 days from the goods (works, services) export date;

6) receipt of the payments for the export of particular goods, the list of which is established by the Government of the Republic of Kazakhstan, by the residents from the nonresidents, if the period between the goods export date and export proceeds receipt exceeds 365 days;

7) granting credits for the period exceeding 180 days by the residents (except for the banks) to the nonresidents;

8) charging of the foreign currency received by the resident as a credit from the nonresident to the accounts of the third parties:

9) transfer of the currency values for the asset management by the resident to the nonresident.

It is important to pay attention to the fact that according to the new Rules the new requirements for the subjects applying for the license are established:

- **absence of the tax debts** (shall be confirmed by the relevant certificate from the tax committee);
- **absence of the outstanding debts on the credits** granted from the Republican and the local budgets.

As before, the basis for non-issuance of the license is also the outstanding debts on the credits to the Kazakhstan! banks. Previously, the grace period for the advance payments for the goods on import transactions requiring the license from the National Bank consisted of 120 days. The Rules provide for a new period of **180 days.** The price limit for the export-import transaction requiring the license of the National Bank has been raised from 5 000 to **10 000** USA **dollars.**

2. Currency Transactions Registration

The following is to be registered:

1) currency transactions connected with the capital flow providing for the property (funds) receipt in the Republic of Kazakhstan and/or arising of the obligations for the funds return to the nonresident to the amount exceeding the equivalent of **100 thousand** USA **dollars:**

credits receipt from nonresidents for the period exceeding 180 days including the financial leasing;

crediting of the export/import transactions by the nonresidents:

nonresidents' investments in the Republic of Kazakhstan in the form of direct and portfolio investment including the primary distribution of the residents' securities in the international capital markets including the issue of the depository receipts for the residents' securities;

nonresidents' remittances for the payment of the full transfer of the exclusive right for the objects of intellectual property by the residents;

nonresidents' remittances in return for the property rights for the real estate;

2) direct investments of the residents in the countries of **the Organization for Economic Cooperation and Development (OECD)** and (or) countries, with which the Republic of Kazakhstan has concluded and ratified the international treaties on the mutual investments encouragement and protection, in the result of which the resident making investments will possess fifty and more percent of the voting shares (fifty and more votes of the participants) for the investment object;

3) opening of the accounts abroad with a foreign bank by the resident physical person, if the foreign bank is registered and located in the state, which has a long-term credit rating not less than "A" (according to the classification of Standars&Poor's or Fitch rating agencies) or "A2" (according to the classification of Moody's Investors Service rating agency) and is the OECD member.

Previously, if the advance payment of the nonresident in return for the goods purchased by him from the resident or received by the resident delay of payment in return for the goods imported to Kazakhstan exceeded 120 days, the currency legislation required the contract registration. Now **this period consists of 180 days.**

The registration certificate shall be issued within 10 business days from the date of submission of the complete set of documents. Thereby, **the license of the National Bank** is required for the resident to grant a commercial credit on the export-import transaction or money advance to the nonresident.

Otherwise, when the nonresident grants a credit to the Kazakhstani resident, the **contract registration at the National Bank** is required.

3. Transaction Passport

It is necessary to note that receipt of the license or registration certificate does not release the exporter or importer from (and moreover, it is an obligatory condition for the receipt) the transaction passport, if required.

The transaction passport is one of the documents of the currency control. It shall be filled in by the party of the export-import transaction, which is a **Kazakhstani resident.**

Opening of the transaction passport is necessary for the external economic transactions, the amount of which exceeds **5 000 USA dollars.** The contract should contain the detailed requisites of its contracting parties.

If the goods are paid by the nonresident importer after the goods shipment from Kazakhstan, the contract should contain the **precise terms of the goods return** in case of nonpayment of the goods exported by the resident.

The similar situation is with the case, if the resident importer makes an advance payment for the goods before their importation to Kazakhstan. It is required to specify in the contract the **precise terms of return of money** transferred to pay for the goods imported by the resident.

Our company has a great experience in the legal conduct of the currency transactions and would be glad to perform its services for you in receiving of the registration certificates and licenses for the currency transactions, as well as open the transaction passports.

Draft Law on Production Sharing Agreements Applicable to Offshore Oil Operations

By Vadim Shneyer, Associate (Michael Wilson & Partners, Ltd)

Late September 2003, the National Company KazMunayGas and the Ministry of Energy and Mineral Resources of the Republic of Kazakhstan submitted to the Government of the Republic of Kazakhstan for the proposed Draft Law on Production Sharing Agreements Applicable to Offshore Oil Operations (the "Draft Production Sharing Law") for their consideration.

The Draft Production Sharing Law was apparently prepared by the experts from KazMunayGas and the Ministry of Energy and Mineral Resources of the Republic of Kazakhstan and already agreed with some other State Agencies.

Daniyal Akhmetov, the Kazakhstani Prime Minister, stressed the necessity of such a law at a meeting of the Government of Kazakhstan held on 7 August 2003. He stated "it is necessary to speed up the drafting of a law on production sharing agreements that will account to a maximum extent for the interests of the State in the im-

plementation of new oil projects". Further, he stressed that "such a draft law is now being urgently prepared and will be submitted to the Parliament this year".

The enactment of the Law on Production Sharing Agreements, as well as a number of other normative acts, is encompassed by the State Programme for the Development of the National Sector of the Caspian Sea and which was approved by Government Resolution No 843 of 21 August 2003 ("Caspian Sea Development Programme").

The Caspian Sea Development Programme provides for a number of measures to be carried out with the purpose of ensuring and achieving the rapid development of the Kazakhstani Sector of the Caspian Sea, including the adoption of laws changing the principles of subsoil use, taxation and transportation in relation to offshore oil operations.

Despite the fact that the full text of the Draft Production Sharing Law was not published and is not officially available to us yet, we can assume that this law will materially change the principles of offshore oil operations in Kazakhstan by providing for the mandatory participation of Kazakhstani companies and entities, private or State-controlled, in the production sharing agreements applicable to offshore oil operations and management of oil projects, provided such companies and entities meet world standards and other requirements.

We should note that the idea of ensuring participation of local privately-owned and state-owned entities and companies in the development of oil projects is already actively pursued by the Kazakhstani authorities. Thus, pursuant to the Rules on the Representation of State Interests in the Contracts with Oil Contractors approved by the Government of Kazakhstan on 29 June 2002 (the "Rules"), the National Company KazMunayGas must hold at least a 50% interest in all contracts concerning the development of oil blocks put up for investment tenders announced by the Kazakhstani Government. The Rules also provide that the National Company KazMunayGas determines who will be the project operator, which could be either itself, its subsidiary or any other entity.

The Draft Production Sharing Law will apply only to the procedure for granting the right to conduct oil operations in the Kazakhstani Sector of the Caspian Sea and Aral Sea and, accordingly, will have a very specific field of application.

The authors of the draft suggest giving the draft priority in comparison with other legal acts regulating subsoil use.

More than 30 articles of the Draft Production Sharing Law regulate the procedure for entering into production sharing agreements, the obligations of subsoil users, the order of compensation of expenditures, the distribution of powers between the relevant Kazakhstani State Agencies and other issues relating to the activities of oil investors. We should further note that the Draft Production Sharing Law does not provide for any preferred taxation treatment of production sharing agreements. However, these might yet be included in the amendments to the Kazakhstani Tax Code being prepared now by other State Agencies.

Furthermore, it is unclear whether the new law will have retrospective effect, i.e. apply not only to production sharing agreements concluded after its enactment, but also to production sharing agreements concluded before its enactment.

State officials in their official statements stress the importance of the Draft Production Sharing Law for Kazakhstan. Thus, Kazakhstani Prime Minister Daniyal Akhmetov said at a recent meeting of the Working Group for Improvement of Legislation concerning subsoil use and oil operations on 30 September 2003 that changes and amendments to the legislation would increase the transparency of subsoil use contracts, improve environmental protection and encourage investors to bring advanced technology into the Kazakhstani market and possibly establish domestic production complexes for such technology.

Basing on the available information about the Draft Production Sharing Law, our conclusion is that this law is rather different from similar laws adopted in other CIS countries. In contrast to the laws on production sharing agreements in oil operations adopted in other CIS countries and that are aimed to attract foreign investments, the Draft Production Sharing Law rather seems to be aimed at ensuring the participation in offshore oil projects of Kazakhstani privately and state-owned oil and service companies.

After the enactment of this law, foreign investors will be obliged to share the oil and export profits with the Republic of Kazakhstan. Moreover, they will be obliged to share the operatorship/project management role with National Company KazMunayGas in order to have access to the development of attractive offshore oil projects.

New Joint Stock Company Law in Kazakhstan: Main Distinctions and Legal Effect

By Vsevolod V. Markov, Associate (Michael Wilson & Partners, Ltd)

The new Law of the Republic of Kazakhstan "On Joint-Stock Companies" of 13 May 2003 was adopted and officially published on 16 May 2003.

This law replaced the old Law "On Joint-Stock Companies" of 10 July 1998 effective from 16 May 2003, being the date of its official publication. The adoption of the new law will have certain legal effects on most of the existing joint stock companies in Kazakhstan, in particular they will be required to amend their foundation documents to bring them into conformity with the new law.

There are a number of main provisions in the new law which differ from the provisions of the old law, a summary of which, together with a summary of the main consequences of the new law is given below:

! One of the main changes is that the new law completely eliminates the term an "open joint stock company" and leaves only two (2) types of joint stock companies: a joint stock company and a public joint stock company. This will, of course, oblige all existing open and closed-type joint stock companies to reorganise into joint stock companies, amend their foundation documents and reregister with the Ministry of Justice. Under the new JSC Law, such actions should be carried out within two (2) years from the date of the new law. If after two (2) years the necessary amendments have not been introduced in the foundation documents, then such companies should be either reorganised or liquidated within one (1) year after the expiry of the two (2) year period.

! The qualified majority is now not less than three quarters of the total number of voting shares in a joint stock company or 75%. This used to be two thirds or 66.7%. Most joint stock companies will have to amend their foundation documents accordingly.

! The minimum charter capital of a joint stock company has been increased 10 times and is now 50,000 monthly calculation indexes or approximately US$291,667. All companies, the charter capital of which is less than the above sum, will have either to increase their charter capital or to reorganize into a limited liability partnership or otherwise restructure themselves according to the legislation of Kazakhstan.

The minimum charter capital for public joint stock companies was also increased to 1,000,000 monthly calculation indexes or approximately US$5,833,333. Moreover, shares in a public joint stock company should be sold and purchased only on the organised securities market with some exceptions provided in the new JSC Law. Therefore, public joint stock companies will be obliged to amend their foundation documents as well.

! The new law provides that the founders of a joint stock company should pay the charter capital in full during thirty (30) days from the date when a joint stock company is registered as a legal entity. The old law required that only 25% of the minimum authorised capital should be paid by the date of the State registration of a joint stock company. Accordingly, appropriate amendments should be made into the foundation documents of joint stock companies operating on the Kazakhstani market.

! The procedure for calling and holding general or extraordinary general meetings of shareholders has been slightly changed and this will again cause many joint stock companies to amend their foundation documents accordingly.

! The Shareholders Register now can be arranged and kept only by a registrar, which should not be affiliated to the joint stock company or its subsidiaries. Joint stock companies are no longer allowed to keep their register themselves. Those joint stock companies, which keep registers themselves, are obliged to select a registrar and transfer its relevant documents to the selected registrar within three (3) months from 16 May 2003 i.e. by no later than 16 August 2003.

These are only a few major provisions which differ from the old joint stock company law but it is already clear that most joint stock companies will be obliged to take certain steps in order to comply with the current legislation, as shown above.