



**AMERICAN CHAMBER OF COMMERCE  
IN KAZAKHSTAN**

**IMPROVING KAZAKHSTAN'S  
INVESTMENT CLIMATE:  
BARRIERS TO  
FOREIGN INVESTMENT**

**AMCHAM WHITE PAPER**

**2018**







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**Almaty 2018**



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## Executive Summary

The American Chamber of Commerce of Kazakhstan and its member companies know better than anyone how the government can meet its foreign investment goals. AmCham shares the government's interests in increasing investment, and its member companies both are intimately familiar with both the actual business climate in Kazakhstan as well as with models from the world's top economies.

In 2014, AmCham listed 10 areas where there are significant barriers to foreign investment.

- 1. Rule of Law and Judicial Reform**
- 2. Criminalization of Civil Cases and Legal Uncertainty**
- 3. Corruption**
- 4. Environmental Payments**
- 5. Tax Policy**
- 6. Customs**
- 7. Work Permits and Visas**
- 8. Local Content**
- 9. Licensing for Architecture and Engineering**
- 10. National Chamber of Entrepreneurs**

This report updates these, and adds three more:

- 11. Privatization - Strategy and Balance**
- 12. Intellectual Property Rights - Protecting Investor Rights**
- 13. Currency Controls - Necessary or Counter Productive?**

As well, the report gives snapshots of three industries:

- 14. Oil and Gas - Kazakhstan's Economic Engine**
- 15. Agriculture - Kazakhstan's Underutilized Wealth**
- 16. Healthcare - Protecting Investors and Public Health**

**Rule of Law** is an overarching factor in foreign investment, and the government should focus its efforts on strengthening it. In addition to systemic reform - a challenging task, AmCham encourages the increased use of alternative dispute resolution; refraining from interference in judicial independence; systematic training for judges in business law; creation of an intellectual property court or chamber, and better quality monitoring of judicial decisions.

**Criminalization of Civil Cases and Legal Uncertainty** is closely related, and has had a chilling effect on investment. Businesspeople, and citizens in general, need the information to comply with the law on their own, and should not be subject to criminal penalties for civil matters. AmCham recommends greater consistency in lawmaking; better explanation of laws and regulations; and removing criminal liability for civil or administrative matters.

**Corruption** prevention should be a society-wide effort, not only a focus of law-enforcement. Despite Kazakhstan's progress in combating corruption, corruption is still present in virtually every topic of the White Paper. Many of the problems identified are caused and fed by corruption. Kazakhstan should increase the use of e-government and continue efforts to create arms-length relationships with officials; include business integrity as an objective; and expand preventative measures.

**Environmental Payments** related to gas flaring are out of line with OECD practice, and Kazakhstan should rectify this to encourage the use of best technologies and directly promote carbon reduction and prevention of environmental harm.

**Tax** enforcement should be geared to encouraging investment and should follow a risk-based approach, in particular regarding VAT refunds. It is heartening to see tax officials seeking to follow best practices in international tax policy, but interpretation and implementation require further effort.

**Customs** reform, including the one-window approach and on-line declarations are welcome, and AmCham encourages further reforms, also built on a risk-based approach.

**Work Permits and Visas** remain a nettlesome question for investors. The underlying vision, that foreign workers take jobs from local ones, is mistaken. On the contrary, foreign workers can transfer skills and support world-leading technological innovations, and the government should focus more on improving the local labor force rather than hampering efforts to bring in foreign workers.

**Local Content** requirements, as with work permits, tend to obstruct foreign companies' efforts, and necessity, to bring the best expertise and best practices to Kazakhstan, not only for their own companies, but also to share with local companies seeking to upgrade their own skills. A restrictive approach to local content based on quotas and percentages serves to reduce local competitiveness, and runs counter to the spirit of international free-trade commitments to which Kazakhstan is a signatory.

**Licensing** of architecture and engineering services should be replaced by an inspection and permitting regime, as is widespread in the OECD region. Licensing has been used to restrict usage of foreign experts and their expertise, which could serve to upgrade local engineers and specialists. This is counter-productive.

**The National Chamber of Entrepreneurs** should not be used to cancel out independent voices of the business community. Their status as a government agency, rather than an independent business association, should be clarified.

**Privatization** should be carefully prepared and conducted with due attention to the impact of a broad range of factors. Clear goals and transparency are essential. In particular, the first privatization will establish a reputation, for better or worse, that will remain in subsequent deals.

**Intellectual Property Rights** need more proactive protection, in particular by government procurement agencies, which should ensure that bidders possess the appropriate and legitimate intellectual property rights; and by a better trained judiciary.



**Currency Controls** should not be introduced, as they are inconsistent with steps to promote Kazakhstan as attractive to investment, and will create a cascade of problems for current investors. The existing currency controls are adequate for banking requirements.

**Oil and Gas** is a cornerstone of the economy. The government should pursue more flexible policies to better leverage oil and gas companies' inherent interests and capabilities in the growth of the Kazakhstani economy. At the same time, it should retain the stability clause in oil company PSAs and contracts as a demonstration of the Government's commitment to rule of law.

**Agriculture** has had under-investment or misdirected investment, but is a proper target for economic diversification, as well as to ensure the country's food security. Land reform, social reform in rural areas, subsidized interest rates, and crop insurance will be needed to ease the concerns inherent in the sector. Also, policy should be consistent, as frequent changes undermine the long-term certainty required by investors.

**Healthcare** presents a smaller investment opportunity than areas like petroleum or agriculture, yet it offers the chance to introduce cutting-edge technologies that will improve citizens' wellbeing. Medical training needs to be fundamentally updated, and the Government will need to address currency and political risk for providers of medical services if it is to take advantage of the benefits of public-private partnerships. Legislation needs to be updated to clearly differentiate between generic and counterfeit drugs and improve the regulation of medicinal-like products.

AmCham and its member companies are ready to provide advice and engage in dialogue in all of the above areas, and looks forward to continuing their excellent partnership with the Government in pursuing the mutual goal of improving Kazakhstan's investment climate.



## Introduction

### AmCham and Kazakhstan's Investment Climate

AmCham is committed to seeing foreign investment, and the overall economy of Kazakhstan, prosper. As Kazakhstan's leading business association encompassing both international and local investors, AmCham serves as a platform for current investors to discuss the investment climate before making a final decision to invest in Kazakhstan. Potential investors regularly consult AmCham's Executive Director, Board Members, and member companies. These business-to-business dialogues, the experience and expertise of AmCham member companies, and its independence give AmCham a high degree of credibility. During the past decade, the Government of Kazakhstan has increasingly been open to a dialogue with AmCham.

In 2010, AmCham and the Prime Minister formed the *Council to Improve the Investment Climate*, which meets monthly, bringing together Government Ministers, business leaders and ambassadors, as well as guest speakers from international financial institutions based abroad, monthly for focused practical discussions, covering the issues in this White Paper as well as others.

The Council was created following the *AmCham Economic Policy Program (AEPP)*, begun in 2008, which produced a series of topic-specific White Papers on improving the investment climate for the Prime Minister's Office. The Council was seen as a more immediate face-to-face dialogue to develop and enact the White Paper recommendations advanced within the *AEPP* framework.

AmCham also supports a large number of thematic Working Groups across Kazakhstan, including Groups dedicated to tax, trade and customs, technology, healthcare reform, corporate social responsibility, and foreign investment issues, among other topics. In addition, AmCham conducts four Inter-Ministerial Working Groups created by the Prime Minister to meet monthly with Ministers to resolve specific problem issues. Over the past eight years, AmCham has developed a deep and productive working relationship with the most senior levels of Government.

The above working groups are an invaluable resource for the AmCham advocacy program. AmCham brings the vast breadth and depth of resources represented by its membership and many international partnerships to support the Government of Kazakhstan's ambitious program of economic reforms.

# White Paper Purpose and Structure

## Purpose

This White Paper offers a business perspective on how to increase foreign investment in Kazakhstan, and updates the 2014-2015 White Paper “*Improving Kazakhstan’s Investment Climate: Top Ten Barriers to Foreign Investment*.”<sup>1</sup> It is drawn from the experience of the more than 200 AmCham member companies representing Kazakhstan’s largest foreign investors and are present in nearly every branch of the economy.

The Government of Kazakhstan is increasingly interested in heightened investment, economic diversification, privatization and other factors affecting the business environment, with the 2015 drop in crude oil prices adding impetus. But alongside the greater need, the crisis also reduced available resources and the attractiveness of investment targets, so success will require redoubled efforts.

Many studies by the Organisation for Economic Co-operation and Development (OECD), World Bank, and others offer detailed advice on how to make these goals more attainable. Their work is referenced throughout this paper.

AmCham members provide an invaluable complement to these studies by offering real experience of how announced reforms are actually implemented. If one wants to know what investors think, one needs look no further than AmCham member companies. Indeed, when potential investors consider Kazakhstan, first and foremost they turn to other businesspeople and to AmCham itself for a viewpoint unmediated by political considerations. Roadshows and advertisements on CNN may pique their interest, but they will want to verify this information with business partners already established in Kazakhstan.

The topics covered are a mix of the general, i.e. rule of law, and the specific, i.e. policy and practice regarding gas flaring, as are the recommendations. Some of the issues date from the early years of the country’s independence; some are new.

The summaries and recommendations reflect the experience of AmCham member companies, most of which are already working in Kazakhstan, as compared to a survey of potential investors. As such, they are more anecdotal and less quantitative than related studies by international organizations. Yet it is this direct experience that potential investors often want to hear when conducting due diligence. Where this White Paper lacks detail, AmCham is able to provide additional information at the request of policymakers.

The White Paper is concise, and thus focuses on priorities for improvement. AmCham supports the consensus view that Kazakhstan has the best investment climate in the region, and the country continues to make notable strides in regulatory reform, as recognized by the sharp increase in its ranking to 35<sup>th</sup> place in 2017 from 51<sup>st</sup> place the previous year in the World Bank’s “*Doing Business*” index.

Nevertheless, experience indicates room for improvement to achieve Kazakhstan’s foreign investment objectives. These recommendations are offered in a spirit of partnership, since AmCham and its member companies are committed to the success and better future for Kazakhstan and its citizens.

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<sup>1</sup> Further referred to as the “2014 White Paper” for the sake of readability.

AmCham notes the excellent dialogue it has had with the Government for several years now, and which is itself a positive signal to investors. Most of the topics covered in this White Paper are also the subject of working groups and standing dialogue platforms with the Government, for example the *Council for Improvement of the Investment Climate*, created by the Prime Minister as a monthly dialogue platform with AmCham in 2010.

As such, this paper serves as an *aide-memoire* for these more detailed exchanges. At the same time, it must be noted that AmCham has neither the mandate nor the resources to set and track measurable indicators, so this White Paper should not be interpreted as an AmCham action plan, but rather as information, recommendations, and guidance for the Government to further its objectives with the support of the country's business community.

This Paper offers a broad range of concrete recommendations. However, it should be noted that an overarching recommendation is that policy changes should be viewed holistically. Change that is patchwork or too frequent can create legal uncertainty, which in 2014 AmCham members identified as one of the top barriers to investment. Reforms must be enacted in a consistent and predictable manner.

Maintaining and expanding the channels of communication developed over the past several years between the Government and AmCham is crucial. If the Government deigns to enact some or all of them, AmCham recommends it do so within a dialogue process, continuing the excellent communication with the business community to which the Government has in recent years increasingly committed itself.

## Structure

The 2018 White Paper first reviews the original ten investment barriers identified in the 2014 White Paper. All of these issues have been discussed in the ongoing dialogue with the government through the Council to Improve the Investment Climate and other forums. Some have largely been satisfactorily addressed, while others have been only partially resolved. Others by their nature require sustained attention.

Each barrier will be summarized, followed by a short description of actions taken to address it, with updated recommendations for future action.

The second section discusses three new challenges, along with potential barriers and opportunities. These challenges are related to currency controls, privatization, and intellectual property rights. These are all shared priorities of the Government and business community, and by indicating potential pitfalls, AmCham hopes to contribute to their success.

The third section presents three brief industry perspectives: oil and gas, the industry that serves as Kazakhstan's main economic engine, agriculture, the country's top diversification priority, and healthcare, both a public policy priority and a target for diversification.

The White Paper's Conclusion summarizes AmCham recommendations related to the barriers identified in 2014, as well as new issues that have emerged since then.

**SECTION I**  
**REVISITING THE 2014 TOP TEN BARRIERS**  
**TO FOREIGN INVESTMENT**

# 1. Rule of Law and Judicial Reform

Rule of law underpins nearly all areas of good governance and economic competitiveness, not only foreign investment. AmCham members cannot stress enough that this is the main factor in foreign investment. While it requires more political will and is far more comprehensive than specific policy areas, it is the single indispensable element to all other reforms. In the 2014 White Paper, AmCham members expressed the view that judges are far more likely to side with state authorities, and that judicial independence had weakened in the recent past. AmCham recommended the government:

1. Acknowledge rule of law as an overarching factor in foreign investment, and take measures to strengthen it
2. Increase business-law training for judges
3. Increase alternative dispute resolution
4. Refrain from attempts to influence judges

## Progress

The business community continues to consider rule of law the linchpin to creating a vibrant, attractive investment climate. AmCham members have had mixed experience with courts. Some report that they have been treated fairly, which they say may be attributable to their political clout as high-profile investors. Others have experienced unjust judicial process and decision-making, in which judges clearly had been subject to political influence, bribery or pressure from powerful local business interests. Investors rarely prevail in tax, customs, environmental and other regulatory matters, as courts are reluctant to decide cases against state bodies, regardless of the merits of the claim.

AmCham is heartened to see that ensuring the rule of law is prominently featured in the “100 Steps” initiative (as are other needed measures to spur investment), announced by the President in May 2015. This responds to the first recommendation, in declarative form. To truly improve rule of law requires an effort sustained over years, and the buy-in of a range of people and institutions, inside and outside the government, as has clearly been shown in other countries.

The business community will look for evidence that the policy goals outlined in the *100 Steps* and elsewhere are being effectively implemented, and will share their experience with enquiring investors.

Under the *Civil Procedure Code* introduced in January 2016, the *Astana City Court* and the *Supreme Court* are made courts of first instance for, respectively, regular and large investment disputes. The investment community generally welcomes this legislation. It responds to the general recommendation that judges develop specialized expertise in business matters, and allows partners to focus discussions and specialized training on these courts. AmCham member companies report that they are more likely to get a fair hearing in these courts.

The *Astana International Financial Centre (AIFC)* will have its own legal system and independent financial court based on English Law, in an attempt to create rule of law conditions for investors and key stakeholders. This too is generally welcomed, but there remains some lack of clarity about this court’s jurisdiction.

Investors remain dubious that the concept will be implemented in a way that would allow foreign investors' contractual and legal rights to avoid the impact of an imperfect judicial system. In any case, the *AIFC* courts will likely have no jurisdiction over criminal and administrative matters. Also, by removing any disputes with the Government, virtually 90% of investor cases (tax and customs disputes form the majority of cases) will be removed from *AIFC* jurisdiction. This presumably means that investors will remain dependent on Kazakhstan's overall legal environment in operating their enterprises.

In April 2016, the new law "*On Arbitration*" was passed, expanding the possibility for businesses to use this means of alternative dispute resolution within Kazakhstan. This is responsive to requests from the business community. Judicial practice and interpretation of the law, which contains some unclear wording, will establish more clearly how business-friendly the law is. One AmCham member who used arbitration reported that its local partner ignored the decision, with little recourse, even though arbitrations are intended to be enforceable in court.

The *AIFC* intends to offer arbitration services that can be used by parties to any contract in Kazakhstan, whether or not they are participants in the Center. If it lives up to its billing, this may help bolster rule of law concerning contract disputes.

The Supreme Court as well as international partners such as the American Bar Association have provided some specialized training to judges on matters affecting businesses, i.e. customs, taxes and intellectual property, as well as on English language. However, AmCham members generally do not see much noticeable change in subject-matter expertise of judges, and as the overall tendency is for the complexity of business disputes to increase, see the need for continued efforts.

Aside from additional training, the development of specialized courts in addition to those mentioned above, may be a viable way to improve judges' level of expertise. One such priority court would be a specialized Intellectual Property Court<sup>2</sup>.

Other practical interventions can concretize what may appear to be this abstract topic. These should be explored together with the business community and other stakeholders, but a few examples are worth mentioning.

First, the quality of judicial decisions can be monitored, using methodology developed and tested in other countries. This is a strong indicator of both judicial independence and quality of justice, and can highlight problematic areas, where additional training is needed or where legislation is unclear or contradictory.

Second, a set of courses encompassing the main factors affecting the business climate could be institutionalized at the *Supreme Court's Academy of Justice*, in cooperation with the legal and business communities, with judges undergoing systematic retraining.

At the same time, the sum of the above measures does not equal an independent judiciary, which would require more fundamental and far-reaching reform. Changes to how judges are appointed, disciplined and dismissed would be needed, as would reform of other aspects of the legal system, beginning from law-school education and extending to the country's highest court.

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<sup>2</sup> A specialized Intellectual Property Court, or Chamber, will be discussed below in the relevant section.



## Updated Recommendations

The 2014 recommendations remain relevant today, but are updated to reflect new trends and measures:

1. The “*100 Steps*” in effect responds to the original recommendation, that rule of law be recognized as an overarching factor in foreign investment. AmCham supports the measures laid out in this document, and stresses the need for practice to match policy.
2. Undertake a systematic approach to training judges in business law, via, for example, a retraining curriculum in the Academy of Justice. The business and legal communities may be called upon to contribute to its design and instruction, as appropriate.
3. Introduce practical, measurable means of monitoring the quality of judicial decisions, including trial monitoring and review of decisions, with results informing training needs, judicial practice and areas of unclear or contradictory legislation. Looking only at the balance of how many decisions are decided in favor of a business or the government is at best an indirect indicator.
4. The *A/FC* courts and arbitration center are welcome initiatives. Similar alternative dispute resolution mechanisms should be promoted for businesses outside the Financial Center.
5. Specialized courts and the Astana and Supreme Court Investment Chambers, allow for judges to gain experience and knowledge with complex cases, and are generally welcome.

True judicial independence, which remains the optimal means of addressing rule of law concerns for investors, requires independent, objective means of appointing, disciplining and removing judges (among other measures).

## 2. Criminalization Of Civil Cases And Legal Uncertainty

### Summary

Legal certainty exists when individuals, businesses and government officials know that their actions are consistent with the law. AmCham members noted that government officials with whom they deal are often uncertain whether their actions might be interpreted as illegal, and are thus disempowered from making decisions. The same applies to businesspeople. In some cases, actions that had no malice or ill intent make individuals criminally liable, which obviously has a chilling effect on investors. AmCham recommended:

1. Greater attention to ensuring laws and regulations are consistent, enforceable and understandable
2. A longer period of time between the introduction and effective date of laws, to allow regulations to be aligned and stakeholders to respond
3. More web-based information resources to explain laws.

### Progress

Some progress has been noted, for example, by increasing the criminal threshold for violations regarding environmental and tax matters. However, for large enterprises, these thresholds are still too low to resolve the issue, and the underlying problem remains: that mistakes can be criminalized (while, on the other hand, true criminal intent, if below a certain threshold, is not punished).

AmCham members want a stronger tie to criminal intent for criminal charges to be applied. AmCham members also want the possibility to correct mistakes before criminal charges are considered.

While employees of investor companies continue to face criminal liability, Kazakhstan has not introduced liability for corporations; OECD identifies this as an important anti-corruption measure for countries in Eastern Europe and Central Asia (including of course Kazakhstan), but the logic applies to other corporate wrongdoing.<sup>3</sup> Introducing corporate liability would allow the government to more closely attach the crime to the perpetrator and allay fears by individuals that they may find themselves scapegoated for systemic problems in their companies.

Companies likewise report that government officials often remain reluctant to take decisions, or to change a decision once made when contradictory laws might create the perception that they are improperly favoring a company rather than trying to make a reasonable decision. "This is an important point," one AmCham member said, "Government officials are very afraid of making decisions."

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<sup>3</sup> Criminal liability of legal persons is still rare in former Soviet countries. In addition to the benefits described here, its introduction would likely have a positive effect on business integrity culture. OECD, *Liability of Legal Persons for Corruption in Eastern Europe and Central Asia*, 2015

## Updated Recommendations

The 2014 recommendations remain relevant today with addition of the following:

1. Regulations or laws have too often been proposed with little notice. As effective dates tend to be January 1 of the following year, this short notice is further truncated by the holiday season and year-end activities of important stakeholders.
2. For practice to match policy, legislative and sub-legislative acts should be of high quality, with clear language and explanation, and full alignment with other parts of the legislative base.
3. Judicial uniformity and official interpretation across the country is needed. For instance, in the case of the new investment dispute courts, lawyers have the immediate, basic questions of what are considered investment disputes and investment activities?<sup>4</sup>
4. Recommendations related to criminalization of civil matters are:
  1. Remove or further increase monetary thresholds for civil matters to become criminal, and introduce the need to establish criminal intent
  2. Create criminal liability for legal persons.

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<sup>4</sup> Yelyubayev, Z. "An Investment Disputes Court to Protect Investors' Rights," *Investors' Voice*, April 2016

### 3. Corruption

#### Summary

Kazakhstan has taken many steps to combat corruption, but as with other post-Soviet countries, it started from a relatively weak position. It cuts across all fields, from education and healthcare to enforcing industrial regulations. AmCham recommended:

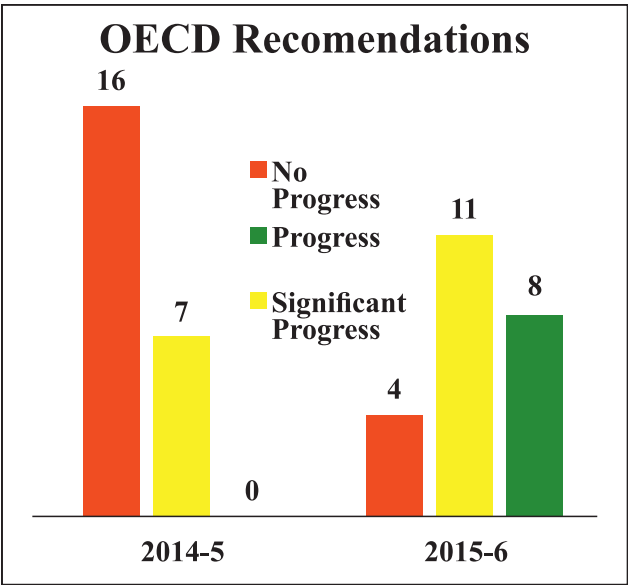
- 1. A society-wide effort, not only a focus on law-enforcement
- 2. Increased use of e-government, detailed explanation of regulations and other steps so that citizens and businesspeople are less reliant on direct contact with government officials
- 3. Positive incentives, such as public recognition, for clean businesses and other anti-corruption efforts.

#### Progress

No AmCham member companies interviewed for this paper reported direct experience of bribe solicitation, extortion or other direct and blatant corrupt practices, which is obviously a positive sign. However, they do believe that corruption continues in subtler ways, for example in rigged procurements or by creating requirements that give unneeded intermediaries chances to make money. Put another way, some of the unnecessary barriers discussed in this report open opportunities for rent-seeking.

Kazakhstan has taken a number of steps to combat corruption, including developing an anti-corruption strategy, reforming relevant legislation and prosecuting government officials for corruption at nearly all levels of government. Despite this, the country's score in *Transparency International's Corruption Perceptions Index* only marginally improved three points, to 29 in 2016, from 26 in 2013, out of 100 This index is both a lagging and indirect indicator, as perception does not always reflect real progress and it may also change later than facts. However, Kazakhstan does not conduct its own monitoring of corruption, which could be more accurate and timely, and more importantly provide a solid basis for guiding anti-corruption efforts, in line with OECD recommendations and with the experience of other countries that have strengthened their efforts.

Whereas the *Transparency* index measures only the perception of corruption, the OECD also assesses national efforts to combat corruption. The OECD's *Istanbul Anti-Corruption Action Plan* includes 23 recommendations, and from October 2015 to 2016 the OECD noted vastly accelerated progress as compared with the prior period, as seen in the chart to the right.



Kazakhstan introduced new laws 1) *On Combating Corruption* 2) *On Public Councils* and 3) *On Civil Service* in January 2016. The first two explicitly widen participation of non-governmental actors in anti-corruption and good-governance efforts, and have seen hundreds, even thousands, of associations and individuals formerly register to participate. However, it is on the whole unclear how much of these efforts are bottom up and how much are top down. In cases where the governmental stakeholder predetermines a main partner, the grassroots effect may be muted. Also, other laws and practice, for example the criminalization of libel and the self-censorship that results, may further limit the potential of grassroots efforts.

The *Civil Service Law* makes a number of significant improvements to public administration overall and to anti-corruption efforts in particular. The new law promotes merit-based hiring and promotion, decreases political appointees, and better addresses corruption and conflict of interest risks. Related legislation and regulations have also strengthened ethics and anti-corruption training. In accordance with recommendation 3 from the 2014 White Paper, whistleblowers are entitled to monetary awards and legal protection.

The *United Nations E-Government Survey* ranks Kazakhstan 33<sup>rd</sup> worldwide in providing on-line services, comparing favorably with Asian and former Soviet countries. On-line services promote government efficiency, reduce citizens and businesses' administrative burdens, and, regarding corruption, negate the need to be in personal contact with officials. At the same time, member companies report that several on-line services are limited. For example, banks may require seeing paper contracts or other documents before processing an on-line payment. While this does not necessarily raise corruption risk, it does reduce efficiency.

Since the 2014 White Paper, AmCham cooperated with the OECD in researching trends in business integrity in the region.<sup>5</sup> In Kazakhstan, the research found very limited incentives from the Government. The study found that international businesses are important in promoting business integrity, as they bring with them well-tested policies and practices; and that investment can also drive better integrity, as preparation and conduct of due diligence provide a direct financial incentive. This new spotlight on business integrity should be utilized and taken advantage of by the Government.

## Updated Recommendations

The original recommendations remain valid. The Government has made a number of anticorruption efforts and aggressively prosecuted many officials; and it continues to make e-governance a priority. Businesspeople report a notable decline in petty corruption, and large foreign companies among AmCham members report that they are rarely asked for bribes. Nevertheless, there is a long road ahead, and as is well known, corrupt practices can shift when one avenue is closed off.

1. The recommendation to involve more actors, including the business community, NGOs and others, in anti-corruption efforts, rather than focus predominantly on law enforcement, is reiterated.
2. Part of this wider effort should encompass promoting business integrity, an area where AmCham is partnering with the OECD and where business associations generally play an important role. AmCham would welcome a discussion with the Government on what public-private initiatives could be undertaken.

<sup>5</sup> OECD (2017), *Business Integrity in Eastern Europe and Central Asia*

3. Increase the evidence-base for anti-corruption policies, including by conducting national research that would include the business and investment community.
4. The expansion of preventative measures could include public asset declarations by government officials. Unlike private citizens, officials need not be innocent until proven guilty, but instead can be screened for corruption risks before or during their employment.

## 4. Environmental Penalty Payments

### Summary

Kazakhstan has one of the worst ecological legacies of any country, and thus properly is concerned with the effects of industry on the environment. However, AmCham members perceive environmental fees and penalties more as a revenue-collection scheme than as protection measures.

Oil and gas companies, Kazakhstan's largest investors, believe they are discriminated against in the taxes, damages and penalties they pay for flaring, as similar emissions from electricity generation, coal, and metallurgy (where domestic companies are more represented) incur less environmental charges. The approach toward flaring also reflects what companies see as the government's approach toward environmental regulation, as a means of collecting revenue rather than protecting and remediating the environment.

AmCham recommended to:

1. Strengthen the effort to rationalize and improve environmental laws.
2. Link monetary damages to actual harm.
3. Remove the multiplied emissions tax as a penalty.
4. Use revenue collected from fees and penalties for environmental restoration.

### Progress

In August 2016, changes to the payment regime lowered costs for flaring, in particular by lowering damages, and introduced the possibility for a company to avoid penalties and damages if it can successfully argue that the flaring was technologically unavoidable. Unfortunately, some authorities, e.g., in Atyrau Oblast, have already begun to circumvent the amendments and are imposing environmental payments in disregard of the new rules. As well, criminal charges can still be brought.

### Updated Recommendations

AmCham continues to believe that the regime used in Kazakhstan is inherently flawed, and recommends instead an approach used in developed countries and outlined by the OECD. A revised approach would include the following elements:

1. Recognize that even using state-of-the art best available technology, flaring is often an unavoidable measure used in response to unpredictable operational conditions. Recent changes that allow a company to argue that flaring under certain circumstances is a technologically unavoidable measure are consistent with this. Imposing penalties, damages and even criminal liability can have a perverse incentive on a safety measure.
2. Cease the use of environmental payments as a source of revenue. It should impose payments no higher than those imposed in OECD-member countries for analogous pollution events. Environmental payments should be imposed as a means of compelling investment in modern infrastructure and ensuring prudent operations using the best available techniques.

**Specifically, AmCham recommends the following revisions:**

**Damages:**

1. As in OECD-member countries, do not impose monetary damages for over-limit gas flaring.
2. Eliminate the indirect method of calculating damages, which is based on an arbitrary formula. Rather, base damages only on physical evidence of actual harm to the environment, and on the cost to remediate or restore the proven environmental damage; give companies the option of performing remediation and/or restoration. In the case of flaring, actual harm is virtually impossible to prove; this would apply primarily to damage to land or water.

**Taxes:**

3. Tax similar emissions from all stationary sources at the same rate, i.e. a molecule of SO<sub>2</sub> from flaring in Atyrau should be taxed the same as a molecule of SO<sub>2</sub> from a coal-fired power plant in Almaty.
4. Eliminate the right of oblast and national authorities to multiply environmental taxes.
5. Eliminate the long list of taxable pollutants in the Tax Code and replace them with a shorter list of chemicals in order to support carbon-reduction and other defined environmental programs. Seek OECD's assistance in this revision.

**Penalties:**

6. Eliminate penalty liability for gas flaring resulting from emergencies and conducted for safety purposes.
7. Eliminate discrimination against gas flaring in emissions penalties: currently, penalties for gas flaring emissions are linked to and hence established based on the discriminatorily higher tax rates in the Tax Code.
8. De-link the calculation of environmental penalties from the emissions rates in the Tax Code and set flaring penalty rates no higher than the rates imposed by OECD countries.

**Criminal Liability:**

9. Decriminalize environmental pollution except where criminal intent is legally established.

Such an approach would also be consistent with public private efforts to apply best available technologies, rather than focusing primarily on end-of-the-pipe measures. This would allow international companies to better employ cutting-edge solutions in Kazakhstan.



## 5. Tax Reform

### Summary

The 2014 White Paper highlighted three separate issues: *VAT refunds*; *double taxation of head office general and administrative (G&A) expenses*; and *royalties*.

Member companies reported long delays in receiving VAT refunds due to the need to show that all suppliers in turn paid their VAT. On this issue, AmCham recommended to:

- Apply a “rule of reasonableness.”
- More promptly grant refunds on VAT that was clearly paid.

Regarding G&A, members noted that tax inspectors had in recent years begun requiring detailed documentation that head-office expenses were related to operations in Kazakhstan. While it is reasonable to require such documentation, members who had been using an indirect methodology for cost allocation found it difficult to comply with requests for prior-year documentation, and in particular for U.S. companies, that reporting needed to follow IFRS rather than GAAP, which is used in the United States. Members recommended to:

1. Allow companies to deduct expenses calculated using the indirect method, prior to the change in practice.
2. Allow GAAP accounting for US companies’ head office expenses.

### Progress

Corporate income and value-added tax rates had been, and remain competitive; the favorable tax regime has broadly remained; and reports of petty corruption attempts have been greatly reduced. AmCham member companies also generally report an improvement in their interaction with tax authorities.

### *Head office expenses*

The complaint regarding head-office expenses in the 2014 White Paper originated from an abrupt change of practice tax offices introduced in around 2010, when they began allowing only directly expensed deductions, rather than indirect, or overhead rates. At the time, companies had difficulty adjusting. It appears that the issue for current tax periods is resolved.

### *Value-Added Tax (VAT)*

Companies report that delays in VAT refunds have in general decreased, but not disappeared. In one well-known recent incident, a major industrial company was obliged to delay payments to its subcontractors as a consequence of a significantly delayed VAT refund. Delays also increase currency risk, with the 2015 devaluation well remembered. As five years or more sometimes elapse between claiming and receiving a VAT refund, multiple devaluations may result in a loss of over 50% of the original value of the VAT payment. For large companies

such as oil companies with VAT refunds of hundreds of millions of dollars in dispute for long periods of time, the financial losses when (and if) refunds are received can be very significant.

The main reason for delays appears to be tax authorities' combating VAT fraud by crosschecking accounts of VAT payers and their subcontractors, and verifying that transactions are legitimate and not financial manipulation. Companies continue to report that this approach results in invasive, weeks-long inspections. At the policy level, the Government has broadly agreed that a risk-based approach to tax investigation is preferred, and has sought advice from advanced economies such as Canada.

This risk-based approach allows the top 300 taxpayers in the country to automatically receive 70% of their refund, but if they claim the remaining 30%, tax authorities then check their entire refund, and can even impose criminal penalties if they then discover part of the 70% was mistakenly refunded. It also allows taxpayers in good standing to be less audited (in line with AmCham's advice). However, other exporters continue to be subjected to the "pyramid" style crosscheck.

From the perspective of AmCham members, actual implementation does not appear to align with that goal, and they believe that officials prefer checklists – this may be partially an effect of lack of legal certainty, discussed above, and may also indicate more thorough training is needed. One member said, "we are speaking different languages about risk management."

While the trends are broadly favorable, a few areas of policy dialogue have raised concern among foreign investors, in particular a discussion about replacing VAT with sales tax (which may have in part been driven by oversensitivity to VAT fraud), and there is a general wariness that the government may introduce business-unfriendly reforms to patch a revenue hole from the oil-price drop. For the time being, VAT is being retained without a countrywide changeover to sales tax.

### ***New Initiatives***

The Government has introduced a range of anti-fraud initiatives, many taking advantage of IT innovations, since the original White Paper. While broadly welcome, AmCham would like the government to consider their impact on businesses' need to update their own systems and practices, and to harmonize where possible reforms, to avoid duplication and unnecessary disruption to business operations.

In 2017, consideration of tax appeals was moved to the Ministry of Finance, a move supported by AmCham. However, as of yet, no formal mechanism exists to allow taxpayers the right to represent themselves to the ministry.

### **Updated Recommendations**

1. Continue with implementation of a risk-based approach to tax issues, in particular VAT. This should be supported by objective interpretation of the law, including considering the risk position at the time of the transaction, not that of a few years later.
2. Consider additional steps to reduce further delays in VAT refunds.
3. In introducing new reforms, take better account of companies' ability to comply by reducing duplication and including reasonable transition periods.

4. Update and harmonize accounting, tax, labor, commercial and civil law related to group restructuring, to allow for smoother corporate mergers.
5. Consider enacting, in legislation and in practice, the “principle of certainty”, acknowledging this should be implemented partially in the 2018 Tax Code.
6. In addition, implementation of a “substance over form” approach together with Advanced Pricing Agreements (APAs) and binding rulings will be beneficial.
7. Develop clear rules on communication between taxpayers and the Appeal Committee of the Ministry of Finance to ensure the position of the taxpayer is understood and considered.
8. While there are many specific areas of tax legislation, interpretation, and implementation open to dispute by investors, the over-riding recommendation has been to view tax policy as a powerful tool to encourage investment, both foreign and local, in Kazakhstan.

## 6. Customs

### Summary

Kazakhstan's geography is a handicap in accessing world trade routes, although the One Belt One Road initiative may improve this. Transparent, simple customs practices can alleviate some of the inherent disadvantages and prepare Kazakhstan to profit from the new Silk Road, yet AmCham perceives deficits in rule of law and corruption. The *World Bank's Doing Business* index for 2018 lowered Kazakhstan's rating for ease of trade to 123<sup>rd</sup> from 119<sup>th</sup>, underscoring that international trade is a stark outlier to the country's generally excellent progress in regulatory reform.

As these are addressed in other sections, the 2014 White Paper focused on the following recommendations:

1. A one-window approach for import and export
2. On-line declarations
3. Clear statement of rules on websites
4. Customs and tax authorities coordinate to prevent double taxation on royalties

### Progress

Kazakhstan became a member *World Trade Organization* in November 2015, in addition to membership in the *Eurasian Economic Union (EAEU)*. The EAEU membership, while removing trade barriers inside the bloc, raised barriers for external trade, with average tariffs increasing, and trade with partners such as the European Union decreasing (in large part due to a decrease in oil prices). EAEU membership gives foreign investors access to markets throughout the block.

This may benefit investors in some sectors, but overall the benefits of EAEU membership to investors, and why an investor would choose Kazakhstan as compared to a different member state, remains a subject for further study. The WTO membership also requires a range of reforms and imposes policy constraints not only in trade and customs matters, but of course on non-tariff measures, i.e. tax regime and subsidy policies.

Kazakhstan started piloting a one window for export and import operations in July 2017; it intends to introduce on-line declarations in 2018; and also in 2018 will allow importers to immediately import their products, filing declarations after the fact. While briefly described here, if implemented in full, these measures will no doubt address the problems with trade that have – in contrast to strong performance in other areas – kept Kazakhstan well behind its stated goals in the *Doing Business* survey.

At the same time, some AmCham members are not overly optimistic about customs reforms, based on the lag in reform compared to analogous areas like tax administration.

They also note the knock-on effects of inefficient import and export procedures. As an example, *KazPochta* (Kazakhstan Postal Service) needs to increase its parcel delivery service to increase its income, and thus attractiveness for privatization. This means largely speeding imports from China; however, it has had difficulty making arrangements to increase this efficiency. In the bigger picture, and stating the obvious, the *One Belt One Road* initiative's benefits to Kazakhstan in part depends on the efficiency of freight forwarding.

### Updated Recommendations

The announced reforms are responsive to the first two recommendations from the 2014 White Paper. Their implementation should be carefully monitored, with recommendations updated based on actual practice after they fully come into effect. AmCham recommends the following additional measures to strengthen customs administration.

1. Give high attention to the rollout of electronic customs declarations. AmCham unreservedly welcomes e-declarations, and recommends the following steps to ensure they achieve their intended purpose:
  - o Explain in detail the processes for electronic declarations on official websites, i.e. user registration and payment conditions.
  - o Pay attention to creating an integrated digital system: export-control documents, certificates of origin and others currently exist only in paper form, which may interfere with the ability to go fully on-line.
  - o In allowing businesses to submit declarations to any customs authority, permit taxpayers to use a single payment account (as compared to the current practice of having a separate account for each region).
2. Introduce a new risk management system as a cornerstone of reform and increase automation. Issues such as determining the customs value, classification of goods, appointment of customs examination and customs inspection should be fully automated excluding the presence of the human factor. Customs officials should instead focus their attention on high-risk, high-return areas of possible fraud, both maximizing their efficiency and reducing interference with business operations.
3. Build an orderly and transparent methodology for conducting customs control after the release of goods (as dictated by new customs legislation), based on risk and reducing the human factor.

The above recommendations are essential to helping Kazakhstan gain ground in this important area, and will require new regulatory acts. These should be prepared in close consultation with the business community.

## 7. Work Permits And Visas

### Summary

Kazakhstan, at a high level, recognizes the benefits that foreign experts and multinational firms bring, yet member companies have complained that work permit laws, visa regulations and the approach of local cognizant officials appears to contradict this.

AmCham supports increasing the percentage of both Kazakhstani workers and content, and argues that making local workers and businesses more competitive via training and capacity-building programs are the most effective way of doing so, and member companies stand ready to assist. Restrictions on foreign workers, on the other hand, are a blunt instrument that negatively affects foreign investment.

The 2014 White Paper recommended:

1. Measures such as extending work permit length, reducing document requirements and enabling visas on arrival are welcome and will greatly facilitate company operations that require specialized qualifications and expertise by foreign workers.
2. Improving the local labor force remains a priority, primarily through general and specialized education

### Progress

Regarding the second recommendation, AmCham members do see concerted efforts to improve educational qualifications for professionals. They offer Nazarbayev University and the Bolashak Program as sources of highly qualified engineers and other specialists. Progress is less apparent, however, in the crafts professions. AmCham member companies continue to support technical and engineering education: one example is the *Kazakhstan Maritime Academy*, which helps prepare local cadets for maritime industry careers domestically and internationally.

Regarding the first recommendation, the situation is more complex. Several improvements to work permits were introduced in January 2017, in line with the first recommendation above.

These include 1) eliminating the need to conduct local market research before hiring a foreigner, 2) increasing the number of permit renewals 3) eliminating a set of “special conditions,” i.e. that permit holders are obligated to train local workers and 4) eliminating the need to report on business trips by permit holders. As well, the exemption for heads of representative and branch offices and companies with large investment projects remains in place.<sup>6</sup>

Another welcome development was the introduction of 2-week visa-free visits for 45 countries, starting from January 2017.

<sup>6</sup> A more detailed list of the changes can be found at Eppner, D. “Improvements to Kazakhstan’s Work Permit Regime.” *Investors’ Voice*, February 2017

At the same time, some of the rules worsened, in particular limiting the permit holder to working in only one *oblast*: for companies that operate in, for example, Atyrau and Mangistau oblast, the logic behind this unnecessary rule is unclear. A three-year renewal was replaced by three one-year renewals, increasing the paper burden. Also, a new requirement was introduced that applicants must receive their permits in their country of origin. For international experts who often work outside their home countries, this creates a burden that serves no apparent purpose other than raising costs for companies.

Also, requirements that had never been justified have remained, in particular regarding formal education requirements. It is not uncommon for workers who could be among the most qualified in the world, with decades of applied experience, to lack formal education degrees in their field. Companies strongly contend that their managers' judgment of employees' qualifications is a sounder basis than formal degrees, which in any event, can be virtually impossible to verify.

Also, it must be noted that there was a set of *proposed* rules legislated and ready for implementation that would have worsened, not improved, the situation. AmCham does not wish to dwell on this near miss, yet, as it illustrates an issue with legal certainty and business-government dialogue, it is worth considering briefly.

The proposed rules included lifting the exemption for CEOs, introducing quotas per country and requiring permit holders to pass a Kazakh-language test. At the risk of understatement, the international business and diplomatic community did not support this package of measures. After emergency consultations with the government in late 2016, the new rules were suspended.

AmCham greatly values the willingness of the government to listen and constructively respond to the concerns of the business and diplomatic community. Nevertheless, it should be noted that their initial development represented a departure from the normally excellent dialogue, which the government pursues with these stakeholder groups.

The planned introduction on New Year's Day, just slightly more than two months after they had become known to the investor community also is an illustration of a deficit in legal certainty, described above, where the timing and advance notice for introducing rules can create confusion among both businesspeople and the government officials charged with enforcing them.

At the same time, the government still makes use of quotas, which appear at times out of line with actual requirements and possibilities. At the risk of over-simplification, in many areas, for example catering or transport, foreign companies can, and indeed prefer to, forego foreign workers entirely.

In other areas, for example, automation engineering, it may take years to develop qualified staff, which is not possible without bringing in the expertise. AmCham knows of examples where a foreign company was forced to move engineering work entirely offshore, as it could not comply with the requirement.

In general, AmCham members see that local officials are trying to promote employment, an understandable and noteworthy goal. However, at times the baby gets thrown out with the bathwater, when for example, quotas kill projects, generating employment neither for foreign nor for local workers.

## Updated Recommendations

1. While noting some improvements, the recommendations from 2014 remain in place.
2. Executives maintain a complete consensus that work permits need to undergo a fundamental liberalization, both on paper and in practice, and that the economic incentive of avoiding costly expatriate hiring and relocation to Kazakhstan is enough of an incentive. "It's not efficient for us to bring expats in. This is not our preference," said one.
3. To avoid the situation with the abortive heavy-handed regulations, AmCham recommends improved dialogue before changes are introduced in the future.



## 8. Local Content

### Summary

Local content requirements, as with work permits, are blunt instruments that negatively affect the efficiency and competitiveness of foreign investments. With the Customs Union, Russian companies can now use Russian vendors to satisfy local content requirements, further negating the original intent. AmCham recommended, rather than imposing quotas, two approaches favored by the OECD:

1. Implement supply-side programs, such as the FDI-SME linkage program.
2. Create more flexible and realistic requirements.

### Progress

The entry into the World Trade Organization (WTO) in 2015 requires Kazakhstan to remove “trade-related investment measures” (TRIMs) which can restrict international trade during a transition period until 2021. TRIMs include local-content requirements.<sup>7</sup> Despite this, the government has announced its intention to continue using local-content requirements as a tool to promote Kazakhstani businesses.<sup>8</sup> AmCham members note that new rules linking local content to a single factor – number of workers employed on a project – and linking local content to work permits have further worsened the situation

AmCham members express the view that while adhering to the letter of WTO – and EEU – commitments, officials may look for ways to maintain current policies. As evidence of this, one reports that the local authorities are *increasing* pressure to sign long-term contracts with local vendors in anticipation that this opportunity will decrease as legislation and practice come into alignment with WTO requirements.

AmCham companies have also noted the continuation of some practices that might charitably be described as inefficient. One such practice is requiring foreign architecture and engineering firms to partner with Kazakhstani companies holding a Category 1 construction license.<sup>9</sup>

On the whole, the recommendation by the OECD, made in 2013, remains as valid today as it was then:

*“The government should take steps to ensure that local content requirements are made more flexible and realistic; that local content and expatriate employment requirements should be made more transparent, and complemented by effective supply side policies to increase the quantity of local inputs and raise their quality; and that regular evaluations of policies should be conducted to assess their effectiveness.”<sup>10</sup>*

<sup>7</sup> The WTO requirements are in part included in the Law “On Amendments to Some Legal Acts of the Republic of Kazakhstan in connection with the Accession to the World Trade Organization,” October 2015.

<sup>8</sup> <http://www.government.kz/en/novosti/28874-within-the-framework-of-wto-kazakhstan-defends-right-to-establish-requirements-on-local-content-m-mirzagaliyev.html>

<sup>9</sup> Also discussed in the “Licensing” section below.

<sup>10</sup> OECD (2013). *Promoting Investment and Job Creation in Central Asia through Business Linkage Programmes*, accessible at [oecd.org/global-relations/BusinessLinkageProgrammes.pdf](http://oecd.org/global-relations/BusinessLinkageProgrammes.pdf)

## Updated Recommendations

The original recommendations remain in place.

1. The principles of the WTO and EEAU are built around widening the market, which will bring economic benefit to countries and industry sectors that are properly positioned.
2. Kazakhstan should redouble efforts to build capacity of local workers and companies, rather than using administrative methods to artificially strengthen their ability to win bids.
3. AmCham and its member companies reiterate their support for the development of local business, both in their desire to see Kazakhstan succeed because it helps their bottom line, and are ready to help the government identify more efficient ways to promote this development.

## 9. Engineering and Construction Licensing

### Summary

Kazakhstan's rise in the *Doing Business* rankings is largely due to a reduction in the number of documents and permissions needed for various business operations. Yet further improvement is needed, in particular in the area of licensing, and the 2014 White Paper pointed to cases where potential investors explicitly avoided or withdrew from Kazakhstan because of licensing problems. AmCham recommended:

1. A review of licensing requirements, including considering foreign experience as sufficient to demonstrate compliance
2. Reducing the overall number of licenses

### Progress

Kazakhstan has made progress in further streamlining the number of licenses and shifting more licenses to on-line. This is reflected, for example, in its remarkable improvement in the World Bank's *Doing Business* category on dealing with construction permits from 78<sup>th</sup> in 2016 to 22<sup>nd</sup> in 2017.

AmCham members too note a general improvement, but continue to at times encounter what they see as an overly bureaucratized approach, with differences sometimes depending on the location of the licensing authority.

For current and potential foreign investors, one of the key issues concerns architecture, engineering and construction projects, which are licensed according to difficulty, with a "Category 1" license needed for complex industrial or large building projects. OECD countries generally do not issue such category-based licenses, but rather seek qualifications based on the project need, and certify the actual construction, rather than the company.

Companies complain that several years of experience in Kazakhstan has been needed for a Category 1 license, meaning that even major multi-national companies have had significant difficulty, while smaller firms have been excluded.

This requirement also has led to cases where Kazakhstan-registered companies with the license (but not the expertise implied by the license) become intermediaries for foreign companies who bring the actual capacity. In some cases, the local company brings needed expertise and other value added. In other, the local company is perceived as an unnecessary and costly intermediary; and in addition to the license, though, foreign partners may need to accept liabilities, overhead and other unattractive elements as part of the package.

In summer 2017, the government announced that the requirements would be changed, to better align with OECD standards. This is a welcome improvement, but it remains to be seen how it will be implemented.

## Updated Recommendations

1. Continue reducing the number of licenses.
2. Concerning public procurement, allow foreign companies to submit information on successful bids in OECD countries as evidence of their qualifications, an approach used by both the EBRD and ADB.
3. For architecture and engineering licenses, continue dialogue with business community and experts from OECD countries on how to transition away from a license-based to a construction inspection and permitting regime; and monitor how the reform is implemented throughout the country, particularly in public tenders.

## National Chamber of Entrepreneurs (Atamaken)

### Summary

At the time the 2014 White Paper was prepared, the National Chamber of Entrepreneurs was still in the process of being established. AmCham raised the concern that mandatory membership and high fees would undermine the Chamber as an independent voice for its membership, since it would not need to demonstrate its value to its members. AmCham recommended:

1. Membership be voluntary, at least for foreign companies
2. The Chamber's functions be clearly separated and not assume governmental functions.

### Progress

The Chamber was registered in March 2015, and is now also known as Atamaken. It imposes mandatory membership and dues on Kazakhstani companies, including those with foreign ownership. It does not require membership or dues of foreign companies. This is in partial alignment with the first AmCham recommendation in 2014

Both the American and Kazakhstani Chambers share the broad goal of improving the business environment, which is self-evidently critical to attracting investment. However, their point of departure, structure, methods, and results are distinctly different.

Atamaken positions itself as increasing the negotiating power of businesses with the government, and among other functions, assists companies with complaints, for example by supporting the Business Ombudsman, and advises on how to reduce administrative burdens. At the same time, it was created by national legislation, membership is mandatory, and its presidium includes Government ministers and Members of Parliament, so it is in reality more akin to a bridge between business and Government than a pure advocacy organization.

Atamaken regularly takes part in meetings with investors while seated with, and at the invitation of, the Government. The Government frequently refers to Atamaken as representing Kazakhstan's entire investment community and seeks its recommendations on a broad range of investment issues. In almost all instances, Atamaken opposes AmCham recommendations and the recommendations of other foreign investment bodies.

Atamaken has members from all-sized companies, but states that its objective is to strengthen the voice of small and medium enterprises, which otherwise might have a weaker voice at the national level. Some AmCham members who are also (mandatory) members of Atamaken confirm that the association has the resources, connections and statutory authority to be an effective lobby. However, there is doubt about whose interests are actually represented by Atamaken. Many of its positions and recommendations do not, in fact, benefit smaller businesses, the business segment that it states it supports.

On issues of local content and work permits, as well as more specialized issues such as intellectual property rights and currency controls, Atamaken tends to take a protectionist position which, in the view of AmCham, does a disservice to its members by substituting recommendations based on the controversial but populist infant-industry argument.

Atamaken's alignment with Government agencies and unspecified interest groups is perceived as a problem compromising its effectiveness as a legitimate business association. This has been recently underscored by its newly-official status to provide obligatory support (or rejection) of draft legislation proposed by other business associations before the legislation is sent to the Majilis.

### **Updated Recommendations**

1. The main concern of AmCham members in 2014, mandatory dues, was addressed for branches and representative offices. Atamaken's role and positions are a matter for its members to determine, so AmCham offers no further recommendations concerning its internal structure.
2. However, AmCham is concerned by Atamaken's positioning itself with Government agencies, uncertain representation of business interests, tendency to adopt a political stance in its decision-making, and lack of expertise in handling complex investment issues. The Government might wish to reconsider the dominance Atamaken currently holds in influencing Government investment policy.

**SECTION II**  
**NEW INVESTMENT CHALLENGES 2018**

## Privatization – Strategy and Balance

Spurred first by large revenues during the period of high oil prices and then by the financial crisis of 2008, the Government of Kazakhstan – primarily via the Samruk-Kazyna National Welfare Fund and later Baiterek National Management Holding - increased its sovereign holdings to at least half the economy.<sup>11</sup> Seven years later, the drop in oil prices further hit the economy, and in particular the state budget, creating pressure to divest.

Kazakhstan has long understood that state ownership is a suboptimal way to manage assets; it has long pursued increased foreign investment; following the oil shock, the Government is looking for quick injections of revenue; and as part of its overarching strategic goal of becoming one of the top 30 economies, it wishes to reduce its public sector to about 15% of the economy.

Hence, in September 2015 the Government announced its intention to launch an ambitious new wave of privatization, with the goal of privatizing as many as 800 state-owned enterprises by 2020, including the 65 largest. The privatization program is too large and complex to be described here.<sup>12</sup> Rather, this paper will focus on the view of AmCham member companies.

In broad terms, AmCham member companies welcome the privatization program, and are aware that the government considers foreign participation essential to the credibility and ultimate success of its plans. At the same time, based on past experience around the world, including Kazakhstan, they are acutely aware of the potential for privatization to fall short of its promise. One AmCham member compared the current situation to the first privatization drive in the 1990s, when the lack of a track record allowed investors to believe the future would be bright. Now, they have far more evidence on which to base their decisions.

AmCham members share the consensus that the percentage of state-owned assets is far too high. At the same time they urge a cautious, methodical approach that recognizes the potential pitfalls. Such an approach would require revising the current government target of reducing SOEs to 15% of the economy by 2020 to a more modest goal spread over a longer period of time.

Whether privatization is successful depends on how success is measured: Is sales revenue the main indicator? Increasing downstream tax revenue? companies' competitiveness? attracting foreign investment? expanding domestic investment opportunities for citizens? improving public services? In some cases, all of the above may be complementary, but in others political decisions will be needed.

Another set of decisions concerns how much companies are able to offload their social obligations before, or after, sale. Reducing workforces, setting tariff rates, providing necessary but unprofitable social services will all require either difficult decisions.

Aside from these political questions are ones more grounded in fundamental political, business and macroeconomic considerations that apply more generally to the investment climate. Some of these, where government can positively intervene, are described elsewhere in this paper: to give just one example, currency controls that complicate the repatriation of profits would lower the attractiveness of any privatization target.

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<sup>11</sup> The government estimates state assets are 40% of the GDP, but others place the percentage much higher.

<sup>12</sup> Official on-line sources include: [privatization.sk.kz](http://privatization.sk.kz) and [top65.gosreestr.kz](http://top65.gosreestr.kz)



Other essential elements are not as generalized to the overall investment climate. At the industry level, in sectors such as power and transport, overall reforms at the sector level would make assets more attractive. Many of the state-owned enterprises require restructuring and reforms prior to privatization; in some cases these are already underway, in others, progress is more difficult.

One of the goals of Samruk-Kazyna's transformation plan has been to allow SOEs in its portfolio to be run like businesses, with the government subsidizing social functions if needed, but these decisions are difficult and may require expenditures to be shifted from the enterprise to the government. To take two concrete examples, KazPochta keeps post offices in remote communities open, even when they are not profitable; and tariffs for electricity is set by the government. While there is clear argument made for providing social services throughout the country, investors will likely hold the opinion that the government, not the enterprise, that should subsidize social goals.

Regarding the privatizations themselves, how they are conducted is essential. Their sequencing, how well the transactions are prepared, the degree of transparency and other factors will all be closely watched, with early successes (and hopefully not failures) setting the stage for later privatizations. AmCham members also predict that for the healthiest companies, in particular ones that occupy strategic sectors, only minority positions will be offered, reducing their attractiveness.

In all these, communication is essential. The government has set good examples of increased communication and dialogue with the business community, and these good habits are critical in privatization. The investment community of course needs to be engaged in dialogue; so too do other stakeholders such as workers and their families, customers and local communities. These dialogues are important in their own right, but they will also ease the entry of new owners and investors.

The above points are at the same time both obvious and very difficult to implement. But they underscore the myriad of factors that will come to the surface when potential investors conduct due diligence on targeted companies.

Without these changes, privatization may favor buyers with political connections, as they will need to manage political questions as much as the businesses themselves.

AmCham and its member companies are ready to assist wherever the government may consider their intervention useful.

A related area is PPPs, which cover a range of services and take a number of forms, from toll roads to offering healthcare services. The revenue hole from the oil-price drop has increased the government's interest in replacing procurements with concessions. However, companies are wary that the time periods required to break even are too long to effectively manage risk without guarantees. These risks include rotation among their government partners and currency risk.

## Recommendations

1. Consider privatization as a step-by-step program, bringing a small number of privatizations to the market fast and building on their success. Investors not only need to become aware of the investment opportunities in Kazakhstan but also become comfortable with the investment environment. Initial success is essential to spur investor interest and a sustained privatization is required to maintain that interest.

2. Designate a single focal point with a high level of political and formal authority and the necessary administrative and staff resources. Realistic and clear metrics, including intermediate targets, should be set.
3. Clearly state the goals of privatization, which will vary among enterprises. Revenue generation is an appropriate goal, but in most cases should not be the main factor, as it represents a one-time gain. Longer-term benefits, including likely sustained revenue streams from taxes, economic productivity and competitiveness, should also be given sufficient weight.
4. Not all privatizations are meant to attract foreign direct investment, but if FDI is one of the goals, several steps will increase the likelihood of success. These include offering majority ownership and clear protection of minority shareholder rights.
5. Transparency of privatizations that creates a level playing field for investors is essential to the success of the overall program. One way to measure this transparency is through the level of investor interest reflected by their participation in the auction process and the range of investors who participate. Absence of foreign competition usually means lack of transparency or poor preparation of the company for the privatization.
6. Prepare enterprises ahead of time. Corporate governance should be strengthened, in particular where only minority shares are offered. If the workforce needs to be restructured to make an enterprise competitive, or if environmental remediation will be needed, this should happen before the sale. Regulatory issues should be addressed in advance.

The above recommendations align with those of analysts and international organizations, views based on the experience of other countries. The OECD, for example, summarizes its, as such:<sup>13</sup>

*“The privatisation programme should clearly state its objectives and be monitored on the basis of appropriate indicators. Offices responsible for privatising assets should be given adequate time and resources to prepare the assets, including due diligence, but also adjustments in the capital structure of the entity and the identification and costing of any public service obligations. The privatization programme should be controlled ex-post by an independent body to ensure a maximum requirement of transparency and accountability, ultimately increasing credibility for investors.”*

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<sup>13</sup> OECD, *Multi-dimensional Review of Kazakhstan: Volume 2. In-depth Analysis and Recommendations, OECD Development Pathways, 2017*

## Intellectual Property – Protecting Investor Rights

Intellectual Property Rights (IPR) are critical to establishing a welcoming investment environment. A potential investor will need to know that its product or service will not be undercut by counterfeits or parallel imports. It is also essential to establishing a modern society, where liability for the safety of products can be tied to a legitimate provider.

Kazakhstan has made much progress in protecting registered trademarks, copyrights and patents in recent years. AmCham has enjoyed constructive cooperation in IPR policy development via the *Inter-Ministerial Intellectual Property Rights Working Group*, which addresses the concerns of the technology, pharmaceutical, and consumer products industries.

In practice, an active rights holder is generally met with support from government authorities when trying to defend its IPR. They regularly report that the customs service notifies them when attempts are made to import goods that potentially violate their IPR, either in cases of parallel imports, when an authentic product is imported but without the approval of the IPR holder, or when a product is suspected to be counterfeit.

However, law enforcement and the courts have been less supportive. The complexities of IPR disputes at times have proven challenging for judges, and law enforcement does not generally recognize the illegality or importance of confiscating pirated or counterfeit products and bringing charges against their manufacturers or distributors. Customs officials have demonstrated a greater level of understanding in this respect.

AmCham members believe further steps could be taken.

First, in government and quasi-state procurements, the purchasing agencies are not required to verify that IPR is protected. As an example, a bidder could offer pirated software in a computer purchase, undercutting a bid with licensed software. Not only is the procuring agency not required to check the license, but also it may give preference to the pirated version if the bid's cost structure is lower. It is then up to the license-holder to monitor procurements and identify IPR infringements on its own.

This laissez-faire approach is not the norm in developed countries, or within EAEU partner Russia.

In the case of software, the procuring agency is violating a company's license. In other cases, for example involving pharmaceuticals, the procuring agency may be risking the health and safety of the population as well as violations of patent rights. A pharmaceutical procurement process that verifies patent rights would be an additional tool in combating this well-known risk.

Regarding counterfeit drugs, the U.S. Department of Commerce, an AmCham partner, has been working with the government of Kazakhstan to improve detection and interdiction. At the same time, AmCham members in the healthcare industry suggest a more comprehensive drug policy is needed to systematize efforts at protecting against harmful medicines and patent infringements.

The courts' difficulty in adjudicating IPR disputes is not a problem limited to Kazakhstan as IP cases can be highly technical and may involve rapidly changing technologies. Other countries have addressed this problem through establishing specialized IP Courts or chambers.<sup>14</sup>

Third, AmCham members see a risk in draft amendments to the EAEU treaty on parallel imports, which at a minimum would introduce uncertainty and may have the perverse effect of increasing gray imports. A bill currently moving through the Majilis legislative process risks legalizing parallel (gray) imports. This draft legislation requires corrective action before it is passed into law.

## Recommendations

1. Continue cooperation and dialogue with the Justice and Healthcare Ministries via the Inter-Ministerial Intellectual Property Rights Working Group
2. Require procuring agencies to verify that successful bids are not violating the rights of legitimate right-holders
3. Consider establishing a specialized court or a chamber of an existing court to focus on IPR matters
4. Include IPR into retraining curricula for judges

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<sup>14</sup> *Specialised Intellectual Property Court - Issues and Challenges* by J. de Werra et al., *Second Issue, Global Perspectives for the Intellectual Property System, CEIPI-ICTSD, Issue Number 2, 2016*, available at: [www.ictsd.org/themes/innovation-and-ip/research/specialised-intellectual-property-courts-issues-and-challenges](http://www.ictsd.org/themes/innovation-and-ip/research/specialised-intellectual-property-courts-issues-and-challenges)

## Currency Controls – Necessary or Counterproductive?

Foreign investors cite their experience of predictable unimpeded movement of capital in Kazakhstan as a key factor in the country's attractiveness. They are highly wary of changes to the foreign exchange regime, and note that an economy so dependent on imports and exports requires a liberal regime.

The National Bank of Kazakhstan earlier in 2017 proposed a draft law on currency controls with the aim of improving macroeconomic stability and promoting greater use of the Tenge. Following the devaluation of the Tenge in 2015, and controversy about how the matter was handled, such policy goals are understandable. At the same time, the government will need to evaluate the degree to which currency controls negatively affect another stated policy goal: attracting foreign investment.

The draft bill contains several provisions of concern to international investors. It expands the definition of resident to include all branches and representative offices of foreign legal entities registered in Kazakhstan. Residents have to use only Tenge in transactions between themselves. The result is additional currency risk for foreign investors conducting operations in Kazakhstan through branches, as such branches will have to use the national currency in their transactions with Kazakh legal entities. Thus, for current investors, an additional problem would be the need to renegotiate hundreds or even thousands of contracts, with the uncertainty that partners would agree to replace dollars or euros with Tenge.

For current investors, an additional problem would be the need to renegotiate hundreds or even thousands of contracts, with the uncertainty that partners would agree to replace dollars or euros with Tenge.

Participants in the Astana International Financial Centre would be exempt (in apparent acknowledgement that the new rules are not investor-friendly).

A number of exemptions are being discussed, some for virtually entire sectors of the economy, others for categories of workers.

However, AmCham shares the international community's consensus that new restrictions on foreign exchange are a policy mistake. AmCham is also concerned that it has had little opportunity for dialogue with the National Bank on this issue. Under pressure from AmCham and the foreign investment community, introduction of the new currency regulations has now been delayed to 2019, allowing more time for consultation between AmCham, the National Bank, and the Government.

### Recommendations

1. Do not introduce new currency controls. These will create a new barrier to foreign investment, and the extent of harm will become apparent only after they are in place.
2. One reason given for the proposed currency controls is to improve statistical information on balance of payments, by separating resident and non-resident payments. AmCham is open to discussing ways to address this gap in statistics, other than introducing currency controls.

**SECTION III**  
**INDUSTRY FOCUS 2018**

## The Oil and Gas Industry - Kazakhstan's Economic Engine

The oil and gas industry was highlighted in the 2014 White Paper as the most prominent area of foreign investment. Accounting for more than half of all exports and foreign direct investment, the oil and gas industry is treated by international investors as symptomatic of the overall investment climate's health. A potential investor in any sector will look to oil and gas for signs of a friendly investment climate.

Also, as the country's main economic engine, this industry has the potential for driving other growth sectors, for example chemicals, and being the proving ground for world-class new technologies. In sum, oil and gas are the bedrock on which economic diversification can be built. The industry experiences many of the problems typically faced by foreign investors, but also faces its own specific issues.

Government policy tacitly recognizes that oil and gas are the economy's key economic drivers. Local content requirements, quotas on hiring Kazakhstani citizens, revenue collected not only through taxes or agreements but also through environmental payments, fines and delayed VAT refunds all attempt to maximize the benefit of the sector to the Kazakhstani economy.

However, these short-term gains are achieved at the expense of the country's long-term interests, and its reputation among investors, for several reasons.

***First, content and labor quotas restrict the ability of companies to introduce new technologies and ways of doing business, and introduce inefficiencies.*** Particularly during start-up phases of new projects, companies require unique expertise and technologies that have never before been utilized in Kazakhstan, and thus may only be available internationally. The government's recent liberalization of work-permit and local content requirements for selected projects recognize this, and are welcomed by the investor community.

It may be worth considering whether further liberalization of labor and content restrictions might also benefit smaller companies or projects with less ability to lobby for exemptions, as well as projects at other phases of development.

***Second, local content requirements and quotas support an overly bureaucratized attitude of government officials toward businesses,*** where inspections and varied interpretations of rules replace a systematic regulatory approach and supportive attitude by government officials. Nearly all companies interviewed for this White Paper said the procedure for issuing or rejecting work permits was opaque. One AmCham member with foreign workers said that when a candidate is rejected, the company is not informed of the reason why, and has to make further inquiries.

Also, AmCham members note that the requirements often do not match the real world. For example the requirement for academic credentials does not take into account that a master craftsman may have decades of literally irreplaceable experience, but no university degree.

***Third, there is a high perception of arbitrariness in the enforcement of rules.*** This is at odds with the strengthening of rule of law, considered by both investors and international organizations like the OECD as the overriding barrier to foreign investment. Taking gas flaring as an example, oil companies are concerned that monetary damages are not proportional to actual environmental harm, as is the practice in most developed economies. Rather damages appear to be assessed to increase short-term revenue and to apply leverage or



punishment for matters unrelated to environmental protection. And they see that collected damages are not spent on environmental restoration, undermining the contention that the intention is to mitigate or punish ecological harm.

***Fourth, preferential treatment virtually never leads to a competitive domestic industry.*** Aside from the many academic studies disproving the “infant-industry” theory, Kazakhstan’s own experience suggests that quotas and limits do little to promote industries adjacent to oil and gas production. Meanwhile they support industries like garments, where Kazakhstan does not have – and likely does not want or need – a competitive advantage.

Regarding developments since the 2014 White Paper, petroleum companies are concerned that while specialized courts and chambers may protect investor rights, they are nevertheless subject to vagaries regarding a range of labor, environmental and economic cases, as well as to inconsistent practices across different courts.

***As with other industries, proposed currency controls are of concern to the oil and gas companies,*** but they acquire particular significance in that the increased controls will require them to renegotiate hundreds if not thousands of agreements within their value chains, introducing uncertainty and a high administrative burden.

Of particular concern to the oil industry is the Government’s stated intention to remove the stability clause in the production sharing agreements and contracts with the major companies, thus opening the way to renegotiate other contractual terms that would impact negatively on the industry. The stability clause is the foundation on which many of the contracts signed with the Government in the early 1990’s - and later - are founded. To remove stability would be a major blow to the oil and gas leaders’ relationship with the Government and their faith in rule of law as a major tenet of their ability to work in Kazakhstan.

It remains to be seen whether stability will remain in the contractual negotiations that will take place with the major oil companies in early 2018, and in the future.

## Recommendations

1. AmCham agrees entirely with the Government’s policy goals of more and better jobs for Kazakhstanis and of diversifying the economy.
  - However, AmCham recommends that more flexible policies could better leverage oil and gas companies’ inherent interests and capabilities in the growth of the Kazakhstani economy. Any company making a multi-billion-dollar investment that will only produce returns many years later has an ironclad incentive to support a stable, prosperous society characterized by a diverse economy.
  - As leaders of industry, oil and gas companies have supported Kazakhstani business development both indirectly, through payments to the national treasury, and directly through support to institutions that train thousands of workers, and through introducing the world’s best technologies.
2. AmCham strongly supports retention of the stability clause in oil company PSAs and contracts, which is simultaneously a demonstration of the Government’s commitment to rule of law.
3. AmCham opposes additional currency controls that will negatively impact on the oil industry and their multitude of local suppliers, as well as on many other foreign investors in Kazakhstan. Adequate currency controls are already in place and no additional controls are needed.



## Agriculture - Kazakhstan's Underutilized Wealth

Kazakhstan is the world's ninth largest country by landmass, and much of this land is arable with a high agricultural potential. It is not surprising that the government places agriculture at the top of its diversification priorities list and hopes the agriculture sector will be a "new driver of the economy," according to the country's official 2050 Strategy.

The government admits, and specialists agree, that the sector is far below its productive capacity. Costs and capital expenditures tend to be high, with many agricultural inputs needing to be imported. In Almaty – the grandfather of the apple – markets are stocked with Chinese apples, and despite the titular nation's nomadic traditions, livestock that produces competitive yields must be imported at several thousand dollars a head.

Agriculture, food processing and related industries are all identified as having high potential for economic growth, exports and investment, and are the target of several government programs and policy declarations. While the country is a main exporter of flour and wheat, it is generally a net importer of fruits and vegetables. The One Belt One Road Initiative will help open up Western China for products where Kazakhstan can demonstrate a comparative advantage.

Land ownership has proven to be one of the most difficult reform areas for the government of Kazakhstan. It is not the purpose of this White Paper to analyze the socio-political reasons for why this has issue has proven to be so emotionally charged, but rather to offer some practical recommendations.

In spring 2016, the government announced a new attempt at reform with two key elements. First, citizens would buy land rather than lease it. Second, legal entities with up to 50 percent foreign ownership could lease land for up to 25 years, an increase from the prior limit of 10 years.

These two streams would have had obvious economic benefits. Landowners would gain collateral to better access credit. Both owners and leasers would have stronger incentives for responsible land management. And new prospects for investment, both foreign and domestic would be opened up.

However, the reform sparked protests by citizens suspicious that the competitive sale of land would be unfair or inaccessible to farmers and that it would open the door for foreigners to acquire large parcels of land. A common complaint was that the reform had been introduced with inadequate communication and dialogue.

Social problems such as poor educational opportunities and an inadequate social safety net, underdeveloped infrastructure, and a poor perception of economic opportunities in agriculture are also endemic to rural communities and villages, driving young people away to seek better opportunities in major cities and urban areas. Thus, the most capable human resources are lacking for agricultural development.

Another problem is that with uncertain policies and a lack of transparency in state-owned enterprises, it will be difficult to conduct well-founded valuations of investment targets.

Still, investors see potential at other points in the value chain. Irrigation systems, precision-farming technologies and generally more equipment all have good potential. Food processing likewise is seen as an area with wide horizons.

## Recommendations

Even without land reform, there are attractive areas for foreign investment in agriculture. The government is correct in prioritizing this as an area for economic diversification, but the many systemic barriers that have so far contributed to under- investment in this sector will need to be addressed if this potential is to be realized.

AmCham therefore recommends the Government:

1. Improve education and social support in rural areas in order to retain young people on the land to develop agriculture and agribusiness.
2. Legislate land reform in a form acceptable to the rural population and Kazakhstan's population at large that will open up land ownership opportunities to encourage agricultural development.
3. Exercise caution in introducing and ending targeted programs, as frequent changes create uncertainty for investors. As an example, *Agribusiness 2020*, with a number of market-support instruments like interest-rate and investment subsidies, was replaced well before 2020 by a different program when the minister changed.
4. Provide subsidies of interest rates. Without crop insurance and stability in agriculture policies, commercial banks are unable to provide credit to agriculture.
5. Establish effective crop insurance programs to reduce exposure to risk.
6. Give equal access to government assistance to foreign investors as well as local companies, recognizing that international companies can bring innovation and new approaches essential to closing the crippling efficiency gap in the country's agriculture.

## Healthcare - Protecting Investors and Public Health

Pharmaceuticals, medical equipment and other healthcare industries are considered strong prospects for investment, and both overall and targeted government programs recognize the need for improvement in healthcare provision. The government has encouraged an increase in locally-produced medicines, requiring modernization and new construction of production facilities, while recognizing that the market in Kazakhstan is limited and may be more efficiently served by imported medicines from a variety of international sources.

As with other sectors, rule-of-law, corruption and other issues are cross-cutting. Two issues are worth highlighting specific to this sector.

Concerning pharmaceuticals, Intellectual Property Rights and Protection are central concerns in Kazakhstan that the Healthcare Ministry has not yet adequately addressed. Patent violations, gray imports and illegal dietary supplements (which claim medicinal properties) pose a direct health risk and are ongoing concerns that AmCham has sought to address through its Inter-Ministerial IPR Working Group . Three issues regarding pharmaceuticals deserve attention.

**First, the government and quasi-state agencies are the main procurers of drugs, yet they do not verify that bidders are the legitimate patent-holders.** This poses a risk to consumers and at the same time creates the need for patent-holders to constantly monitor procurement results and, if necessary, to initiate court proceedings after the fact. When the Ministry is informed of patent violations in the procurement process, the response is to assign responsibility for detecting these violations to the patent-holders, rather than to the Ministry.

Recent efforts by the Government to reform the healthcare procurement process have resulted in the removal and prosecution of procurement staff. While this is a positive sign that Government commitment to reform, it reflects poorly on procurement to date in a sector crucial to public health and well-being.

**Second, although pharmaceutical companies report a cooperative approach from officials** when counterfeit drugs are discovered in local pharmacies, nonetheless counterfeit medical products continue to be sold, in particular on the Internet, and advertised in Kazakhstan. As with other areas of IPR, a relatively new and complicated area for many countries, drug companies note that further training of court and law enforcement personnel could be beneficial.

**Third, pharmaceutical companies recommend that legislation and regulation be updated** to address areas where greater clarity is needed, for example concerning herbal supplements, and by closing loopholes in IPR law. There is persistent confusion by officials, even by healthcare officials, between “generics”, i.e. legitimate and authorized copies of drugs whose patents have expired, and counterfeit drugs of dubious quality produced from unlicensed sources not subject to Government inspection.

Regarding medical devices, the government is promoting public-private partnerships as an alternative to purchase of equipment. As an example, rather than purchasing a magnetic resonance system, the government would instead invite a company to provide the service in exchange for a usage fee.

Such arrangements typically require several years to achieve the targeted return on investment. However, several barriers exist to making this idea a reality. First, while the central government is promoting the partnerships, local governments would typically be the purchasers, and companies are concerned about their dedication to the approach, in particular as leadership rotates. Second, fees need to be pegged to a hard currency, as devaluation could destroy expected profit margins.

Medical-equipment suppliers note that if such partnerships become feasible, it may increase their interest in investing in manufacturing capacity inside Kazakhstan.

AmCham has more than a dozen leading international member companies primarily operating in the healthcare sector, and many divisions of major companies present in Kazakhstan. These companies have been providing advice to the Government on healthcare reform, and are ready to continue to do so to find solutions to the sector-specific and general barriers identified in this paper.

## **Recommendations**

1. Require the government and state-owned enterprises to verify that successful bidders hold rights to the proffered intellectual property.
2. Update and refine legislation to clearly differentiate between generic and counterfeit drugs and improve the regulation of medicinal-like products, i.e. herbal supplements.
3. Put in place mechanisms to cover currency and political risk for providers of medical services, to take full advantage of the benefits of public-private partnerships.

## Conclusion and Summary of Recommendations

A major improvement to Kazakhstan's investment climate will require deep and consistent reforms. Implementing 70% of reforms will not necessarily translate into a 70% improvement in the actual climate, as many are linked, and all depend on strong rule of law.

While special privileges for investors are no doubt welcome, doing business in Kazakhstan, or any country, requires that the overall environment is healthy. Predictability is also needed: reforms need transparency, dialogue and consistency with each other, not rapid emergency measures.

With these caveats – that rule of law and a transparent, systematic approach are fundamental – the Recommendations from AmCham and its members in this 2018 White Paper are collated here.

### Rule of Law and Judicial Reform

Rule of law is an overarching factor in foreign investment, and the Government should focus its efforts on strengthening it.

1. Increase alternative dispute resolution; the AIFC courts and arbitration center are welcome initiatives.
2. Refrain from attempts to influence judges.
3. Undertake a systematic approach to training judges in business law.
4. Introduce practical, measurable means of monitoring the quality of judicial decisions.

### Criminalization of Civil Cases and Legal Uncertainty

Businesspeople, and citizens in general, need the information to on their own comply with the law, and should not be subject to criminal penalties for civil matters.

1. Pay greater attention to ensuring laws and regulations are consistent, enforceable and understandable.
2. Increase intervals between the introduction and effective date of laws, to allow regulations to be aligned and stakeholders to respond.
3. Expand web-based information resources to explain laws.
4. Legislative and sub-legislative acts should be of high quality, with clear language and explanation, and full alignment with other parts of the legislative base.
5. Judicial uniformity and official interpretation across the country is needed.
6. Remove or further increase monetary thresholds for civil matters to become criminal, and introduce the need to establish criminal intent.
7. Create criminal liability for legal persons.

## Corruption

Corruption prevention should be a society-wide effort, not only a focus of law-enforcement.

1. Increase use of e-government and give detailed explanations of regulations and other steps so that citizens and businesspeople are less reliant on direct contact with government officials
2. Introduce positive incentives, such as public recognition, for clean businesses and other anti-corruption efforts.
3. Add business integrity as a focus area of anti-corruption efforts.
4. Increase the evidence-base for anti-corruption policies
5. Expand preventative measures that could include public asset declarations by government officials.

## Environmental Payments

Kazakhstan should adopt practices consistent with OECD countries, to encourage the use of best technologies and directly promote carbon reduction and prevention of environmental harm. The current policies and practices do not meet these goals.

1. Recognize that gas flaring is at times unavoidable for safety purposes, and should not be penalized, consistent with practice in OECD countries.
2. Environmental payments should be imposed as a means of compelling the use of best practices, not for the purpose of generating revenue.
3. Damages should be imposed for actual harm to the environment.
4. Tax emissions from all stationary sources at the same rate.
5. Eliminate the right of oblast and national authorities to multiply environmental taxes.
6. Base policy on a short list of chemicals to target carbon reduction and other defined environmental programs.
7. Eliminate penalty liability for gas flaring resulting from emergencies and conducted for safety purposes.
8. Eliminate discrimination against gas flaring in emissions penalties
9. De-link the calculation of environmental penalties from the emissions rates in the Tax Code and set flaring penalty rates no higher than the rates imposed by OECD countries.
10. Decriminalize environmental pollution except where criminal intent is legally established.

## **Taxes**

Include tax reform and tax policy in the overall Government strategy to encourage investment.

1. Develop tax legislation and policy with due consideration to attracting further investment, both foreign and domestic.
2. Continue with implementation of a risk-based approach to tax issues, in particular VAT.
3. Consider additional steps to reduce further delays in VAT refunds.
4. Update and harmonize accounting, tax, labor, commercial and civil law related to group restructuring, to allow for smoother corporate mergers.
5. Consider enacting, in legislation and in practice, the “principle of certainty.”
6. Implementation of a “substance over form” approach together with Advanced Pricing Agreements (APAs) and binding rulings will be beneficial.
7. Develop clear rules on communication between taxpayers and the Appeal Committee of the Ministry of Finance.

## **Customs**

Plans to introduce a one-window approach and on-line declarations are welcome, and AmCham encourages further reforms that will facilitate customs clearance.

1. Properly focus on the announced reforms of a one-window approach for import and export and on-line declarations to ensure their successful rollout
  - Explain in detail the processes for electronic declarations on official websites.
  - Pay attention to creating an integrated digital system
  - Permit taxpayers to use a single payment account.
2. Introduce a new risk management system as a cornerstone of reform and increase automation.
3. Build an orderly and transparent methodology for conducting customs control after the release of goods.

## **Work Permits and Visas**

The underlying vision, that foreign workers take jobs from local ones, is mistaken. On the contrary, foreign workers can transfer skills and support world-leading technological innovations.

1. Streamline procedures for issuance of work permits and visas for foreign specialists.
2. Improve the local labor force through general and specialized education
3. Engage AmCham in dialogue on rationalizing this area of policy.

## **Local Content**

The Government should comply with the spirit of its free-trade commitments. Attempts to lock-in local vendors ahead of the WTO effective dates should be carefully monitored.

1. Implement supply-side programs, such as the FDI-SME linkage program.
2. Create more flexible and realistic requirements.
3. Redouble efforts to build capacity of local workers and companies, rather than using administrative methods to artificially strengthen their ability to win bids.

## **Licensing**

Continue reducing the number of licenses. For architecture and engineering, adopt OECD best practices instead of a licensing regime.

1. Concerning public procurement, allow foreign companies to submit information on successful bids in OECD countries
2. Transition away from a license-based to a construction inspection and permitting regime.

## **National Chamber of Entrepreneurs/ Atamaken**

The Government should recognize that the Chamber is not a fully independent voice for the entire business community, and should not be used to cancel out other more independent voices.

## **Privatization**

The first privatizations will be closely watched, with success improving investor confidence. Thus, they should be carefully prepared and conducted with due attention to the impact of a broad range of factors entailed by privatization. Clear goals and transparency are essential.

1. Consider privatization as a step-by-step program, bringing a small number of privatizations to the market fast and building on their success.
2. Designate a single focal point with a high level of political and formal authority and the necessary administrative and staff resources.
3. Clearly state the goals of privatization, which will vary among enterprises.
4. Not all privatizations are meant to attract foreign direct investment, but if FDI is one of the goals, several steps will increase the likelihood of success. These include offering majority ownership and clear protection of minority shareholder rights.
5. Transparency of privatizations that creates a level playing field for investors is essential to the success of the overall program.
6. Prepare enterprises ahead in advance of the privatization.



## Intellectual Property Rights

1. Continue cooperation and dialogue with the Justice and Healthcare Ministries via the Inter-Ministerial Intellectual Property Rights Working Group.
2. Require procuring agencies to verify that successful bids are not violating the rights of legitimate right-holders.
3. Consider establishing a specialized court or a chamber of an existing court to focus on IPR matters.
4. Include IPR into retraining curricula for judges.

## Currency Controls

The introduction of currency controls is inconsistent with steps to promote Kazakhstan as attractive to investment, and will create a cascade of problems for current investors.

1. Do not introduce additional currency controls. The existing controls are fully adequate.
2. Consider rules to separate resident and non-resident payments, to address the question of collecting statistical information.

## Oil and Gas

AmCham supports economic diversification, but also views the oil and gas industry as the cornerstone of these efforts.

1. More flexible policies could better leverage oil and gas companies' inherent interests and capabilities in the growth of the Kazakhstani economy.
2. Retain the stability clause in oil company PSAs and contracts, which is simultaneously a demonstration of the Government's commitment to rule of law.

## Agriculture

The government is correct in prioritizing this as an area for economic diversification, but needs to address the many systemic barriers that have so far contributed to under-investment.

1. Improve education and social support in rural areas in order to retain young people on the land to develop agriculture and agribusiness.
2. Legislate land reform in a form acceptable to the rural population and Kazakhstan's population at large that will open up land ownership opportunities to encourage agricultural development.
3. Exercise caution in introducing and ending targeted programs, as frequent changes create uncertainty for investors.

4. Provide subsidies of interest rates.
5. Establish effective crop insurance programs to reduce exposure to risk.
6. Give equal access government assistance to foreign investors and local companies.

## **Healthcare**

Healthcare presents a smaller investment opportunity than areas like petroleum or agriculture, yet it offers the chance to introduce cutting-edge technologies that will improve citizens' wellbeing.

1. Require the government and state-owned enterprises to verify that successful bidders in the procurement process hold rights to the intellectual property they are offering to supply.
2. Update and refine legislation to clearly differentiate between generic and counterfeit drugs and improve the regulation of medicinal-like products, i.e. herbal supplements, that make medicinal claims.
3. Put in place mechanisms to cover currency and political risk for providers of medical services, to take full advantage of the benefits of public-private partnerships.

## **Continuing the Dialogue**

The above findings and recommendations are offered in the spirit of partnership. AmCham members are invested – literally and figuratively – in the success of Kazakhstan, and look forward to continued dialogue with the Government of Kazakhstan on the points raised above.

**The American Chamber of Commerce in Kazakhstan thanks its many Member Companies and the International Institutions that contributed to this White Paper, presented to the Government of Kazakhstan in 2018.**

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