

IV Investors' Voice

The American Chamber of Commerce in Kazakhstan

Kazakhstan's Leading International Business Association



February 2019

WINTER ISSUE #82

www.amcham.kz

WINTER TAX AND LEGAL PERSPECTIVE - NEW CHALLENGES, NEW APPROACHES



► NCOC - Judicial Recourse in Environmental Inspections

► EY - Tax Code Guidance and Decriminalization

► Baker McKenzie – Kazakhstan's New Currency Law: Commentary

► KPMG - Taxation of Corporate Reorganizations

► Deloitte - Kazakhstan's Taxation Environment and Alignment with International Practice

► Integrites – Enforcing Foreign Arbitral Awards

► Visor – The Caspian Sea Convention:
The Geopolitics of Caspian Pipelines, Oil and Defense

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EDITOR'S NOTE



Dear Readers,

The *Winter Issue of Investors' Voice* is traditionally devoted to new *Tax and Legal Issues* that have emerged over the past year, and this Issue remains faithful to the tradition. We present articles for our readers by leading experts from the Big Four audit firms, leading financial firms, and prominent law firms that enquire into and comment on a broad range of tax, financial, legal and judicial questions of critical importance to Kazakhstan's investment climate.

To set the stage, our first article by U.K. Ambassador Michael Gifford reviews the benefits and challenges of tax reform in Kazakhstan, a speech that was delivered at the January 2019 session of the *Council to Improve the Investment Climate*, AmCham's monthly dialogue platform with the Prime Minister of Kazakhstan and a panel of Cabinet Ministers responsible for the country's economy and judicial system. The Ambassador's speech is followed by three articles from KPMG, Deloitte, and PricewaterhouseCoopers outlining items in the Tax Code that often lead to tax disputes, which too often proceed into the courts, entailing lengthy litigation.

Commentary from Baker McKenzie on Kazakhstan's new Currency Law also relates to a topic covered at the Council last year as investors sought further consultation on new foreign currency regulations that risk complicating financial and administrative operations for many companies. A Deloitte article on reclaiming assets from debtors in bankruptcy court covers an area of law not well-known to the business community. Kazakhstan's Environmental Code and decisions imposed by environmental inspectors (with penalties) are difficult to challenge in the courts despite the Code's inconsistencies by comparison with OECD standards – a subject for an article from the North Caspian Operating Company (NCOC).

A fascinating article from Visor International examines the Caspian Sea Convention signed in 2018 by the Caspian littoral states and illuminates both the terms of the Convention and its geopolitical implications. The past twenty years have been fraught with uncertainties over the Sea's international legal status, preventing full access to the Sea's oil and gas resources, but the Convention represents the latest step in regulating the rights of the five states bordering the Caspian Sea, a process that will no doubt continue.

The February Issue thus contains articles on issues of importance to our readers' work and advances their understanding of Kazakhstan and the Caspian region, its economy and legal framework, its challenges remaining to be resolved in the future.

Doris Bradbury
Executive Director

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Michael Gifford took up his appointment as Her Majesty's Ambassador to Kazakhstan in January 2018. He joined the Foreign and Commonwealth Office (FCO) in 1981 and has had a range of postings in the Middle East, Asia and Europe. He served as Deputy Head of Mission in Cairo from 2001 - 2004 and British Ambassador to Yemen from 2004 - 2007. In London he has worked on Middle East and counter-terrorism issues as well as acting as Deputy Director for property asset management for the FCO.

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TAX REFORM IN KAZAKHSTAN – BENEFITS AND CHALLENGES

by Michael Gifford
British Ambassador to Kazakhstan

For any government, few areas of economic policy give rise to so many opportunities, and present so many challenges, as taxation. Kazakhstan is no exception. The new tax code introduced in 2018 contains many positive changes, and it was good that the Kazakhstan government consulted widely before publication. Local businesses will benefit, and foreign investors, whether from the United Kingdom, the US or elsewhere, will welcome the ambition to simplify the tax regime for small and medium-sized enterprises, to cancel some ineffective tax incentives in accordance with World Trade Organization requirements, and introduce new principles in tax administration.

According to the new code, from January 2019, the type and frequency of tax audits will be based on a clear risk assessment. It is widely hoped that applying a risk-based culture across all aspects of tax administration will do a great deal to improve the investment climate - providing the implementation is done correctly. For Kazakhstan to see the benefits of the new approach, the State Revenue Committee will need be as clear as possible about exactly how that assessment will be made. For example, if a green rating means fewer audits, then that rating should be linked to those demonstrating international best practice.



The new code contains a number of other welcome changes, and as with any new piece of legislation, it is perhaps too early to understand its effect fully, especially as investment decisions have a long lead-in time.

However, there are some tax issues, which still worry foreign investors. One of them is the concept of criminal liability as applied to taxation. Protection of business from unlawful administrative pressure and criminal prosecution

threats was one of the issues addressed by President Nazarbayev in November 2018, when he gave instructions to raise the thresholds of criminal liability with regard to tax violation, and to increase fines.

Corresponding amendments to the legislation were quickly approved, in January this year. However, many independent tax experts and others in the business community would have welcomed a more comprehensive consultation prior to the creation of these amendments.

While the proposed increase of the threshold for criminal liability for unpaid tax is welcome, the suggested amount of approximately \$360,000 is still low for large and even medium-size international companies. At the same time, the increase in fines is a significant burden for businesses.

A more appropriate approach could be to have a threshold - say 10% - that represents a percentage of all taxes paid during the audited period.

Moreover, the amendments do not specify the period that the amount should cover. It seems obvious that the amount of underpaid tax assessed following an audit covering a five-year period will be significantly higher than that for one year.

It is also important to recognize that tax violations committed by companies are often simply the result of differing interpretations of the Tax Code between taxpayers and the authorities. It is essential when assigning criminal liability, to distinguish between intentional tax evasion and misinterpretation of the tax law. And of course, some violations are simply the result of genuine error.

There are other areas that also require clarification, such as the amendments to Article 245 of the Criminal Law Code on the exemption of company executives from criminal liability in relation to the voluntarily settlement of underpaid taxes and fines.

The United Kingdom exported some £2.8 billion worth of goods and services to Kazakhstan in 2017, and we are the sixth biggest investor here. UK-based subsidiaries of US companies are at the forefront of this business, particularly in the oil and gas sector. Getting the basics of the tax rules right - in particular continuing to develop and reform the tax code in a transparent and consultative way - will stimulate trade and investment with Kazakhstan from the United Kingdom and beyond, as well as benefit Kazakhstan's domestic economy.



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ACHIEVING SUCCESSFUL TAX AUDITS AND AVOIDING LITIGATION: TAX CODE GUIDANCE AND DECRIMINALIZATION

**by Erlan Dosymbekov, Managing Partner
EY Kazakhstan and Central Asia**

In this article, two issues are raised that can either predetermine the successful result of a tax audit or become one of its most severe consequences. The first issue concerns written clarifications from the tax authorities upon taxpayer requests. The other deals with criminal liability applied when a tax assessment exceeds the threshold established by Article 245 of the *Criminal Code*.

On the tax authorities' clarifications, which they must provide under Article 19 of the *Tax Code*, the concern has always been that these clarifications are not binding. Thus, there is no guarantee that their position on a specific tax issue will remain unchanged. Having said that, Article 8 of the *Tax Code* was amended in 2018 in what we understand to be an attempt to protect a taxpayer from any changes to a previous clarification from the tax authorities. As a result, there is now an exemption from administrative fines and late payment interest for a taxpayer whose clarification was later corrected, or withdrawn, or replaced with a different one. It should be noted, however, that this exemption only applies if there is a positive resolution to the taxpayer's appeal, and it does not extend to criminal liability.

Even though this may appear to be a positive change, taxpayers are still concerned that this provision in practice may produce repercussions. Firstly, we have seen cases where the tax authorities claimed they are only obliged to issue (binding) clarifications if a taxpayer is on electronic monitoring or has an investment contract in accordance with Articles 134 and 135 of the *Tax Code*. To clarify this approach, we raised this issue with the Ministers of Economy and Finance, as well as the State Revenue Committee (SRC). Both Ministers and the SRC confirm that Article 8 of the *Tax Code* containing the exemption is general in nature and therefore available to all taxpayers, whether or not they fall under Articles 134 and 135.

There is another issue, however, that is much more difficult to resolve. It is only during the actual audit that a taxpayer normally learns that a previously issued position of the tax authorities is no longer applicable. Thus, the SRC tax auditors may disagree with the previous position, resulting in penalties and fines for the taxpayer. The taxpayer would then need to launch a formal appeal process, which may or may not be successful. The only way a taxpayer can protect himself in this situation is to secure a formal withdrawal of the tax authorities' clarification in advance, which would be very difficult, if not impossible.

Our recommendation to both the Ministers of Economy and Finance, as well as the SRC, was to amend the *Tax Code* Article 8 to make its application unconditional and irrevocable whenever there has been a change in a previously issued position. In practical terms, the exemption should always be available even if a written withdrawal of the tax authorities' clarification is missing, which we believe will happen in the vast majority of cases. Furthermore, not only should a taxpayer be exempt from administrative and financial sanctions, but criminal liability should not apply either.

We voiced the same recommendation to the Prime Minister at the *AmCham Investment Environment Council* meeting in January.

As regards criminal liability in so far as it applies to taxpayers, there have been changes to the *Criminal Code*, Article 245, marking some progress in our long-standing debate with the authorities about this issue. More specifically, the threshold for a criminal case initiation has increased from 20 to 50 thousand times the MCI. Furthermore, the reference to a violation being committed "for the first time" as a condition for exemption from criminal action to apply has been removed. As a result, the provisions of Article 245 will now only apply upon an assessment in excess of 50 thousand MCI, whereas the responsible corporate officer could still be exempt from criminal charges even if the underlying violation is committed more than once.

While at first glance these changes appear to be positive, the following concerns remain for most, if not all foreign investors. Firstly, the 50 thousand MCI, which is the equivalent of USD 330,000, is still very low and in many cases will likely be exceeded. In the absence of a proper mechanism for establishing intent, criminal proceedings almost always kick in automatically, thus subjecting honest taxpayers to this disproportionately harsh punishment. Furthermore, for the Article 245 exemption to apply, the responsible corporate officers must "admit wrongdoing", after which the charges will be dropped. This means these officers will still have a criminal record.

We have repeatedly recommended the key stakeholders on the Kazakh side to get rid of criminal liability as it applies for tax violations, particularly in view of very high financial sanctions imposed by the administrative legislation. The latter have been even further increased, which, although in itself this is very negative, it contributes to our argument that Kazakhstan's financial sanctions are high enough for taxpayers to be relieved from any other penalties, including criminal action.

Unfortunately, this proposal has not been accepted by the Kazakh side, and as a result, we have suggested introducing a number of alternative/ interim measures. One of these suggestions was increasing the threshold to a reasonable level using a different basis than MCIs. One alternative is an amount calculated as a percentage of the overall tax liability for the reporting or audited period. Another alternative is to establish a “white list” of law-abiding taxpayers to whom criminal proceedings should not in principle be applicable. Obviously, this list would include large foreign investors and global multinationals.

One more option would be to apply the provisions of Article 245 only if income is concealed, which would normally indicate intent to commit tax evasion. Other tax underpayments stemming from clerical mistakes or misinterpreting tax authorities’ guidance should not be viewed as tax evasion triggering a criminal case. However, even though these recommendations have been extensively discussed with the Government, no improvements have been made to date.

On a positive note, based on our most recent discussions with the Minister of Finance and SRC Chairman, we understand the Economic Investigation Department (EID), which is responsible of conducting criminal investigations of tax violations, is undergoing change. According to both the Minister and Chairman, this change should entail significant improvement. The investigators will now have different KPIs aimed at “resolving matters”, rather than boosting the number of criminal cases initiated in a given year.

Other changes in process will make the EID approach to criminal investigations more reasonable and transparent. While all of this may sound promising, the new system is yet to be introduced and tested in practice. Therefore, at the time of this writing, we are not in a position to comment on whether the EID application of the Criminal Code will materially improve. In the meantime, we intend to continue arguing aggressively on behalf of foreign investors that full decriminalization of the tax legislation should be enacted to ensure no criminal liability applies to bona fide taxpayers.



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KAZAKHSTAN VAT UPDATE: CONTINUING ISSUES

**Michael Ahern, Tax and Legal Head
Partner, PricewaterhouseCoopers**

Current VAT issues

VAT has always been problematic for taxpayers in Kazakhstan, yet important for government as a revenue generator. Although there are numerous current VAT issues, in this article we discuss the following two:

- *Re-audits of VAT refunds, and*
- *VAT applicability to B2B bonuses.*

Re-audit of VAT Refunds

Historically, VAT refunds in Kazakhstan are problematic and difficult to obtain. Tax authorities need to verify the legitimacy of transactions as well as ensure the absence of VAT fraud by cross-checking taxpayers and their subcontractors (the so-called *System of Risk Management via Pyramid Checks*).

Using this system, tax inspectors can check a taxpayer's subcontractors to the level they deem necessary (e.g. the 20th layer of subcontractors). If a supplier in the chain is liquidated, bankrupt, or has errors in VAT returns, then VAT is not approved for a refund. Not surprisingly, VAT refunds are often significantly less than the amount initially claimed.

However, a new problem for the taxpayer has emerged. Several years after approving a VAT refund, the tax authorities may re-run the Pyramid checks and arrive at a different refund amount. Various reasons for this exist (e.g. a mistake made by the inspector during a previous audit, revisions to the Pyramid system, etc.) If the refund amount is lower, the tax authorities will issue a notification requiring the taxpayer to reimburse the difference *with penalty interest*.

Concerns about the legitimacy of VAT re-audits undermines whatever level of trust exists in the VAT administration system. It contradicts the *principle of taxation certainty* and undermines the Tax Code and good tax practice worldwide. As taxpayers have no control over the VAT refund process or Pyramid checks, it is unfair to punish the taxpayer for errors made by inspectors during the (original) audit. Penalty interest should only apply if the taxpayer violated legislation and underpaid taxes, which is not the case in this situation.

The basis for a re-audit needs to be legislated clearly and applied accordingly. Taxpayers should not be responsible (i.e. penalized) for any errors or actions of the tax authorities.

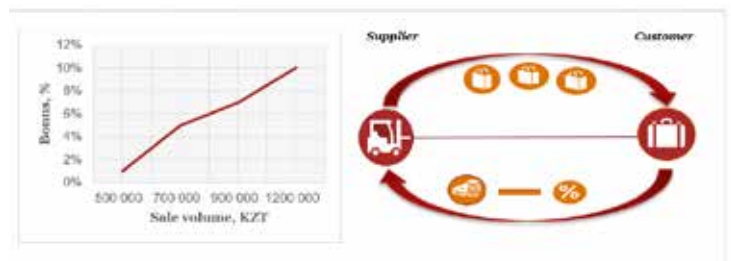
B2B Rebates (Bonuses) That Do Not Change Price Terms: Should VAT Apply?

In many sectors of the economy, rebates or bonuses are provided by a supplier to a customer if the latter achieves specified targets (e.g. volume targets, monetary sales or service levels, etc). In simple terms, they are a monetary incentive for purchasing a specified quantity of goods. *They do not envisage the performance of any extra activities either by the customer or supplier.*

However, the tax authorities have a different understanding. They consider rebates received for purchasing this quantity of goods as remuneration for services delivered. As such, in their view the services attract 12% VAT.

From a technical perspective, it is necessary to understand if the provision of bonuses requires provision of a service and/or performance of work. Neither the *Tax Code* nor the *Civil Code* provides an explicit definition of *work* and/or *services*. However, the Civil Code defines a *provision of services contract* as when:

- The provider performs services ordered by the customer (i.e., undertakes the performance of certain acts or carrying out of certain activities), and
- The customer agrees to pay for such services.



The *Agreement on Indirect Taxes within the Eurasian Economic Union (the EEU Agreement)* prevails over domestic law. It applies to transactions between residents of member states. The EEU Agreement has the following definitions for works and services:

- *Work* – an activity, the results of which have a tangible expression and can be implemented to meet the needs of legal entities and (or) individuals;
- *Activity* – business and other activities (including the supply of services and production of goods) by legal entities, branches, representative offices, and individual entrepreneurs;

- *Services* – an activity, the results of which have intangible expression and are implemented and used in the course of the activity, as well as the granting of patents, licenses, trademarks, copyrights, or other rights.

Given the above, a performance of work and/or services requires that:

- *A customer places an order for certain activities to be performed by a supplier;*
- *The activity is performed by the supplier;*
- *The remuneration for executing the activity is paid by the customer.*

The customer does not perform any work and/or provide any services for the benefit of a supplier if:

- *The supplier does not require the customer to perform any extra activities and no extra activities are undertaken;*
- *The purchase of goods is initiated by the customer (not the supplier) within the customer's core activities (e.g. retail or wholesale);*
- *Bonuses are granted because the customer purchases a certain quantity of goods.*

Considering the above, a bonus (rebate) is a specific form of remuneration that does not involve the execution of any specific extra activities by the customer for the benefit of the supplier. Moreover, the current approach to the document flow for the provision of bonuses (rebates) is associated with:

- *A large administrative burden, and*
- *A mismatch between accounting and tax accounting treatments.*



There are two methods for dealing with bonuses (rebates) in terms of paperwork, both of which are problematic:

- *Method 1:* An additional tax invoice issued by the supplier to the customer. This method is associated with a substantial administrative burden since the supplier's earlier tax invoices need to be corrected for the bonus amount with respect to each delivered stock-keeping unit. Moreover, this method disregards the fact that bonuses should not change the price of supplied goods;
- *Method 2:* The customer issues a tax invoice to the supplier for bonus amount, which leads to a mismatch between accounting and tax accounting since, in tax accounting, supplier bonuses are treated as expense, while in accounting they reduce the gross revenue of the supplier.

In Russia this issue was resolved in 2013. Bonuses in Russia are not treated as a performance of work/services and are not subject to VAT, so long as the bonuses do not change the price terms for supplied goods. Also, in Russia they have a simplified document flow to back up the bonuses with no requirements to show a link between the bonus amount and the price for each delivered unit.



Overall, a similar practical approach needs to be developed in Kazakhstan. Bonuses are not a service that require VAT to be imposed, and the current practice is a waste of time for both business and the tax administration.

The above VAT issues continue to be of concern and require a fresh examination and a fresh approach on the part of the tax authorities as they proceed in their re-examination of VAT implementation and Kazakhstan's Tax Code, which undergoes on-going adjustment on an annual basis. Investors and tax experts are ready to assist in this process with reference to best international practices.

KAZAKHSTAN'S TAXATION ENVIRONMENT AND ALIGNMENT WITH INTERNATIONAL PRACTICE

by Anthony Mahon

Cross-Border Tax Partner, Deloitte Kazakhstan

Kazakhstan continues to make progress towards cooperation and alignment with international tax community; yet, the divergence from fundamental international tax principles continues to exist. International tax practice is becoming more harmonized globally and more advanced in reaching consensus-based tax solutions. Value stands to be lost from the Kazakhstan economy insofar as the country does not similarly implement consistent rules and global practices that are clear, unambiguous, and applied in a straightforward and transparent manner.

Key drivers of the tax uncertainty created by local taxation system relates to:

- (i) *Tax Code provisions that are inconsistent with international standards or insufficiently clear;*
- (ii) *Approach of the state authorities in interpreting tax legislation that is significantly out of line with the guidance set out by the Organization of Economic Co-operation and Development (OECD); and.*
- (iii) *Burdensome tax administration practice.*

A combination of these issues correlates to increased cost and unpredictable risks for taxpayers, thus undermining the country's investment potential. The outflow of economic benefits occurs either when non-residents inflate the costs of their services to incorporate additional tax costs applied in Kazakhstan or by withdrawing from the market.

With this in mind, special attention should be given to improvement of domestic taxation rules that currently expose businesses to an unnecessarily uncertain tax environment.

Tax Code provisions contrary to international taxation principles

A key principle used in international tax law as regards the avoidance of double taxation is that of "*beneficial ownership*". This concept is a key measure in combatting certain forms of tax evasion employing intermediary recipients of income and is included in the *Model Double Taxation Conventions of the OECD, the United Nations and the United States* that serve as a basis for the majority of international double taxation treaties.

The term "*beneficial owner*" was introduced into the provisions of the *OECD Model Tax Convention* regulating the taxation of passive income, i.e. dividends, interest and royalties (Articles 10, 11 and 12) to address difficulties

arising from the use of the words "paid to ...a resident". In the context of respective treaty provisions, the reduced tax rates on passive income are only available to income recipients if they are beneficial owners of such income.

In line with prevailing international tax practice, Kazakhstan's Tax Code provisions governing international treaty application concerning interest, dividends and royalties stipulate beneficial ownership of income as one of the obligatory conditions to access double tax treaty benefits.

However, in addition to the long-standing provisions related to passive income, the new Tax Code effective from 1 January 2018 introduced beneficial ownership requirements with respect to all types of income of non-residents from sources in Kazakhstan. The challenging area in automatic application of the treaty for a tax agent in Kazakhstan is now to ensure that non-resident recipients of all types of Kazakh-source income, including the active income, are beneficial owners.

Firstly, the new provision is inconsistent with the international approach of business profits taxation that provides taxing rights to the active income recipient's country of residence. Moreover, it does not explicitly require recognition of the latter as beneficial owner.

Secondly, local tax legislation is unclear in terms of burden of proof placed upon taxpayers. There is no guidance on documentation required to maintain or procedures to perform in order to sufficiently demonstrate beneficial ownership. Hence, the absence of concrete guidelines provides scope for the tax authorities to deny treaty exemptions, resulting in unfair and unnecessary time and financial costs imposed upon tax agents.

Finally, the beneficial ownership concept is still widely debatable at the international level and a lot of targeted work is taking place to make the concept globally coherent. The diverse application of the concept would ultimately intensify the gap between domestic and international interpretations. This, in turn, would result in global developments toward harmonization becoming irrelevant and not applicable to Kazakhstan legislation.



Improper use and interpretation of legislation

Another common issue is the state authorities' interpretation and application of taxation principles that contradict both international and local legislative provisions. This dysfunction is currently widely illustrated in relation to the issue of "permanent establishment" – one of the most important, yet subjective, principles of international taxation and determination of inter-jurisdictional taxing rights.

The local Tax Code and international treaties set the criteria defining when the activities of a non-resident trigger creation of permanent establishment subject to registration and taxation. The domestic legislation and many treaties provide that permanent establishment exists if a non-resident renders services through its personnel present in Kazakhstan for more than a certain time threshold. The tax authorities use different and inconsistent approaches in performing tests under this provision.

Thus, there are several cases where the authorities considered the length of the contract rather than the physical presence of personnel as a key factor determining creation of a permanent establishment. In other cases, the state authorities apply the proper approach assessing the time spent by a non-resident's personnel in Kazakhstan.

The controversial position was also expressed relevant to the treaty provision on a building site or construction or installation project, or supervisory services connected therewith that create a permanent establishment only if such site or project lasts or services continue for more than certain period of time. The authorities' interpretation of the this provision implies that rendering of supervisory services connected with building site or construction located in Kazakhstan will lead to creation of a permanent establishment even if such services are rendered outside of Kazakhstan.

Although the *OECD Commentaries* on this provision does not set out prescriptive guidelines with respect to supervisory services, the presence of non-resident entities on the site is regarded as a crucial condition in evaluating the constitution of a permanent establishment. For example, the existence of a permanent establishment of subcontractors is assessed based on their activities' duration on the site. Additionally, the period of the site existence starts from the date on which the non-resident begins his work in the country.

The recognition of services performed offshore as activities triggering permanent establishment in other country may contradict OECD guidelines, including the principles of contract aggregations that require commercial and geographical coherence of projects. The main reason for different interpretations of permanent establishment provisions is that the concept requires the application of

significant and specialised judgement resulting in different case-by-case outcomes.

It is important to also consider the detail of OECD Commentaries that provide an analytical guide and comprehensive framework for tax treaty interpretation and its harmonized application.



Burdensome and unfair tax administration

The bureaucracy level in current taxation systems represents one of the main concerns exposing taxpayers to increased administrative and tax costs.

The application of the treaty benefit requires compliance with complicated formalities such as annual provision by a non-resident of the apostilled tax residence certificate of a due form within tightly prescribed timeframes. Treaty benefits may be denied on the grounds of non-compliance with one of the administrative requirements, for example, the late provision of the timely issued certificate due to the lengthy legalization process. All-too-often local tax administrations seem to be seeking ways to deny treaty benefits to taxpayers rather than simply making sure that non-residents are eligible for treaty benefits.

The authorities' form-over-substance approach forces the taxpayers to withhold taxes at their own expense. In practice, the only present solution for companies is to go through the long-lasting procedure for tax refund / credit.

In order to eliminate the highlighted challenges, Kazakhstan's government needs to consider effectively addressing the above matters by (i) amending the contradicting provisions, (ii) incorporating perspectives and examples of international best practice and (iii) developing new ways to simplify burdensome administration.

The *OECD Report on Tax Certainty* issued in 2017 indicates enhanced cooperation between tax administrations and taxpayers as the practical approach in responding to the tax uncertainty.

The overarching objective of collaborative work (using effective and inclusive communication platforms) should be to develop solutions to problematic matters in a manner that both protects the economic interests of Kazakhstan and improves the attractiveness of Kazakhstan's investment climate - ultimately contributing towards effective realization of the nation's strategic reforms.

KPMG - TAXATION OF CORPORATE REORGANIZATIONS

Rustem Sadykov, Partner
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Corporate reorganizations have become an increasingly relevant topic in Kazakhstan in the last decade, leading to the question of how entities involved in reorganization transactions, as well as their shareholders, should be taxed.

Historically, Kazakhstan's tax laws have barely addressed corporate reorganizations and the tax implications these transactions invoke. The present tax law only discusses the procedural aspects of discharging a tax liability to the newly formed or surviving entities in a corporate reorganization. In addition, the tax law provides certain rules for some tax attributes, such as tax overpayments and input VAT and their transfer from one entity to another, but falls short of discussing the transfer of other tax attributes – such as net operating losses, for example.



It is expected that the existing set of tax rules related to corporate merger and division arrangements will be expanded further this year, although at the time of writing this article the corresponding legislation has yet to be voted on in the Senate. The new rules, expected to be enacted on January 1, 2019 (provided that the Senate votes to do so), are designed to clarify issues relating to newly formed or surviving entity assets in corporate reorganizations.

While both the above topics (i.e. the transfer of tax attributes and determination of the transferee's tax basis) are critical tax areas, the existing tax law unfortunately does not clarify whether corporate reorganizations in principle represent a realization event for income tax purposes. More specifically, Kazakhstan's tax law at present overlooks tax-free corporate reorganizations altogether and fails to provide guidance on treating these reorganizations differently from basic asset or share sale transactions.

The Concept of Tax-Free Corporate Reorganizations

From a tax perspective, the notion of a *corporate reorganization* encompasses the vast array of corporate rearrangements in which assets of one entity are transferred to another entity, as happens in corporate mergers and divisions. Moreover, corporate reorganizations may result in the transferor entity's assets being retained by this entity itself but controlled by new shareholders. Investments in kind and share-for share exchanges entail this result.

There are many reasons why businesses carry out corporate reorganizations. While some of these transactions truly represent, both in form and in substance, a sale of shares in or assets of a business, some corporate reorganizations resemble such a sale in form only, not in substance. This category of corporate reorganizations does not technically represent a realization event from a tax perspective; thus, an increasing number of jurisdictions worldwide design a specific set of tax rules that allow taxpayers to conduct tax-free corporate reorganizations.

There are different reasons why a corporate group of companies might wish to pursue a corporate reorganization that does not involve any realization of a gain but is conducted purely for internal reasons. For example, such rearrangements may expand into new businesses or service lines or abandon pre-existing businesses that are not sufficiently profitable. Sometimes businesses may even be forced into a corporate reorganization in order to meet changing regulatory requirements.

From a tax perspective, the main technical dilemma related to corporate reorganizations, such as mergers and divisions, is deciding how to treat the gains and losses resulting from share or asset transfers. In an ordinary asset or share sale transaction with a third party, such a transfer is treated as a realization event with the corresponding taxable gains or tax-deductible (creditable) losses being realized by the transferor. However, if the contemplated reorganization anticipates continuity of control by the transferor after the reorganization, it could technically be argued that, although the arrangement looks like a sale in appearance, it does not represent a genuine realization in substance.

The *continuity of control* test is a critical concept that serves to explain why treating a corporate reorganization that meets this test as a tax-free transaction is methodologically justified and represents a fair tax treatment. This concept requires that, in substance, a substantial part of the value being transferred in the reorganization is still preserved within the same corporate group and continues to be

controlled by it. This principle could be properly applied to any type of corporate reorganization, be it separation-type or consolidation-type mergers and divisions; and to transfers of any type of assets, be it shares, ownership interests, or other assets.

Although they are called *tax-free*, these rules are not designed to grant a tax exemption to any party to the corporate rearrangement. As long as it is accepted and agreed that a corporate reorganization triggers only a change in appearance, but never a change in substance, such rules aim to neutralize the tax effects of the reorganization so that it delivers neither a tax advantage nor a tax disadvantage to any taxpayer involved. These rules serve to allow taxpayers to combine or separate businesses and shift ownership interests within their corporate group without triggering the tax impact on an (as of yet) unrealized gain or loss.

Therefore, deferring taxation in a tax-free corporate reorganization until the resulting gains or losses are realized is never a tax exemption or a tax preference. By the same logic, the purpose of a tax deferral is never promoting or otherwise stimulating corporate reorganizations. The purpose is to effect reorganizations that yield unrealized gains tax-neutral only.

Conclusion

Kazakhstan's tax law has never stipulated any tax-free corporate reorganization rules and, to the best of our knowledge, no such rules should be expected to be introduced into the tax law within the next year or so, despite the business community's extensive efforts to promote this idea and to explain the rationale to tax authorities and legislators. As discussed earlier, the current tax law continues to offer an extremely narrow set of rules with respect to the tax positions of the parties involved in corporate reorganizations. The current lack of detailed and specific tax accounting rules opens up areas for potential disputes with tax authorities, and taxpayers may need to adopt conservative tax positions in their planning and be prepared to face challenges from the authorities.

As Kazakhstan's tax law evolves and becomes more comprehensive and sophisticated, it will presumably begin to address corporate reorganizations in more detail, including introduction of certain tax-free reorganization rules. In the meantime, taxpayers would be well-advised to seek professional tax advice to make an informed decision regarding the tax implications that a corporate reorganization potentially invokes.

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JUDICIAL RECOURSE IN ENVIRONMENTAL INSPECTIONS

by Michael Allen, Head of Government Relations
North Caspian Operating Company (NCOC)

Without a doubt, enacting the right laws can improve Kazakhstan's investment climate. But that alone is not enough. Many of the laws in use today say the right things; some are modeled on analogues that work well in other countries. But how these laws are implemented is important. No less important is the judicial recourse available to investors to protect their rights if the laws are violated.

This article highlights a problem of the latter variety, in which current court practice is in fact denying businesses (and their investors) recourse to the legal mechanisms that exist expressly to protect their rights in disputes with environmental authorities.



Let's take a look at the record to understand the precedents. We were able to find a total of 31 civil court cases in 2017-2018 in which the legality of actions or decisions of environmental authorities were challenged and plaintiffs sought to invalidate an inspection and/or annul the Act of Inspection due to violations of law during the inspection. Of these 31 cases, **87% (27 cases) were summarily dismissed by the courts**, i.e., the merits of the case were never considered.

The cases all concern "gross violations" of *Kazakhstan's Entrepreneurial Code* during inspections by local (Oblast) environmental departments, including breaches of the terms of inspection, or sampling procedures. One of the more problematic of these violations is connected with abuse of powers, or usurping enforcement authority belonging to other agencies.

Despite important changes that have been introduced over the last few years, it has been noted that environmental emission payments continue to be an important source of revenue for local budgets, and fines and damages remain an important performance indicator for enforcement agencies. The *OECD Multi-Dimensional Review of Kazakhstan* in 2017 observed that: "...[E]nvironmental liability in Kazakhstan remains focused on calculating and collecting monetary compensation for the state (essentially serving as a revenue-raising penalty) rather than on preventing and correcting the damage, reducing emissions over time and incentivizing the use of BATs [Best Available Techniques]."

There is hope that reform of *Kazakhstan's Environmental Code*, pursued by the Ministry of Energy in 2019, will address some of these systemic issues over the long term. However, at present and for the foreseeable future, this revenue-raising function is likely to dominate. There is no incentive for executive or judicial authorities to rein in improper practices by inspectors if doing so could result in reduced income to the state budget.

Returning to the question of judicial practice, we note that in 2017-2018 87% of cases were dismissed summarily in courts, citing a lack of jurisdiction over such cases. (NB: There are no other instances for cases of this type in the legal system of Kazakhstan.) When dismissing these cases, the courts often cite what has become a common interpretation of the provisions of *Kazakhstan's Civil Procedure Code* and the Regulatory Resolution of the Supreme Court of Kazakhstan No.8 dated 25 November 2016 "*On Certain Issues of Judicial Application of Environmental Legislation of the Republic of Kazakhstan to Civil Cases by Courts.*"

The interpretation of the 2016 Regulatory Resolution holds that an inspection may not be challenged in court on legal grounds if certain documents – the Protocol of administrative offense or the Prescription for elimination of offenses – have already been issued following the inspection results. The courts reason that failure to submit a complaint prior to issuance of the Protocol and the initiation of administrative proceedings is a procedural omission by the plaintiff's business.

However, in reality, the environmental inspector may serve such documents immediately upon conclusion of the inspection or very shortly thereafter. This leaves little to no time for the business to review the circumstances and file a complaint. Therefore, with no real opportunity to lodge a complaint in time, and with no courts in the land willing to take on such cases, the business investor is left with nowhere to turn for legal recourse.

Inspectors are well aware of this situation and continue to levy fines in this manner with impunity.



We believe the courts' position has led to an unreasonable narrowing of the fundamental rights of all businesses in Kazakhstan, large and small, as regards environmental inspections, due to:

1) Non-applicability of the Resolution

Although courts often cite the 2016 Regulatory Resolution as grounds for dismissing a case, the Resolution itself does not and was not originally intended to regulate challenges to the legal basis of inspections or their results. Rather, one of its tenets (Point 27) is being misinterpreted in such a manner that the unconditional right of a business to appeal an inspection in the Entrepreneurial Code may or may not be granted, depending on how quickly the inspector submits his or her paperwork. This odd circumstance is not encountered in cases involving, e.g., tax inspections. It is only from the (mis-) interpretation of one provision of the 2016 Resolution on judicial application of *environmental* legislation that such problems arise.

2) Administrative Courts should not be ruling in such cases

The *Specialized Inter-district Administrative Courts (SIAC)*, established in 2004, are intended to handle cases concerning administrative offenses, namely, ruling on

whether an offense was committed and the administrative penalties to be applied according to the *Code of Administrative Violations*. Disputes regarding violation of the Entrepreneurial Code during inspections should fall under the exclusive jurisdiction of civil courts, not the SIAC.

What is to be done?

Business is at a dead-end. Whether by specific amendments to legislation or other means, **we believe the State must act decisively to break out of this vicious circle**, to change the existing court practice of dismissing court challenges of environmental inspections, and to ensure that the right to unencumbered and unconditional legal recourse is more than a paper declaration.

This is crucial for Kazakhstan's investment climate. Kazakhstan has in recent years advanced in the World Bank's *Doing Business* rankings, and in general there has been progress towards ensuring control and consistency over government inspections. But this particular issue with environmental inspections is frustrating for investors, current and potential, because major energy and mining investments are highly visible to the public and never far from the watchful gaze of environmental authorities. Indeed, if the right to legal recourse enshrined in the Entrepreneurial Code is not respected, the issue will impact all businesses.



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The Convention on the Status of the Caspian Sea

Geopolitics of Pipelines, Oil and Defence in the Caspian Basin

Michael McNicholas, General Counsel - Visor International Group

The Caspian basin is estimated to hold over 48 billion barrels of oil and 292 trillion cubic feet of natural gas in proven offshore reserves. For more than 20 years uncertainties over the international legal status of the Caspian Sea have resulted in significant portion of the oil and gas resources being stranded.

In August 2018 Kazakhstan, Russia, Iran, Turkmenistan and Azerbaijan came to an accord over the Caspian which has the potential to unlock these resources. But the path to development is not entirely cleared of obstacles.

The “Great Game” – Russo-Iranian Geopolitics in the Caspian

Aficionados of the “Great Game” will know that the Caspian basin has, for centuries, been an important intersection of the geopolitical battle lines in central Asia between Imperial Russia, Persia, the Ottoman Empire and, later, Great Britain.

From the time of Imperial Russia’s conquest of the khanates of Kazan and Astrakhan in the 1560s to the dissolution of the USSR in 1991, Russia has been the dominant military power on the Caspian.

The *Russo-Persian Treaty of Friendship of 1921* and the *USSR-Iranian Treaty of Commerce and Navigation of 1940* effectively divided the Caspian Sea between the USSR and Iran. The treaties excluded any third party, and in particular, the military forces of third parties, from the Caspian, allowing the free movement of each country’s ships throughout the Caspian Sea and establishing an exclusive 10 nautical mile territorial zone for each country. The issue of resource rights was not addressed in any of these treaties.

The collapse of the Soviet Union in 1991 and the emergence of the newly independent states of Kazakhstan, Turkmenistan and Azerbaijan brought control and ownership of the Caspian back into question. The discovery of vast commercial deposits of oil and gas in the region made these issues particularly important.

The Caspian Sea Convention (2018)

On 12 August 2018 leaders of Kazakhstan, Russia, Iran, Azerbaijan and Turkmenistan met in the small seaside city of Aktau, Kazakhstan to settle this question by signing the *Convention on the Legal Status of the Caspian Sea*¹ (the “Caspian Sea Convention”).

The Convention seeks to clarify the rights of each of the five nations to fish and marine resources, surface navigation, the use of the sea-bed and exploration and development rights over the vast oil and gas deposits yet untapped.

However, it is not time to pop the champagne corks for the start of any new projects. Many difficult legal issues await resolution before new oil wells are drilled or pipelines laid in the Caspian.

Why has it taken so long to reach an agreement?

Freedom of the Seas and Maritime Sovereign Territory

From the 15th century onwards international legal convention has recognized that the seas of the world are free to all nations but belonging to none (the “*mare liberum*” principle). Accordingly, no state has the right to control navigation, transit or the use of natural resources in any of the world’s seas.

From the 17th century it came to be held that, as a matter of customary international law, each nation’s sovereign rights extended over a belt of water extending beyond a state’s coastline. Initially this was commonly viewed as 3 nautical miles based on the principle that the effective range of a shore-based cannon was 3 nautical miles, and therefore this was the limit of the territory over which a state could effectively exert control and assert its sovereignty.

With the advance of time and technology the 3 nautical mile limit proved an unsatisfactory protection to the environment, fisheries and marine resources and adjacent territory. Some states unilaterally sought to enforce greater and greater territorial rights and to chase off all other nations from any activity in their sovereign economic zones – effectively “gun-boat diplomacy”.

Various treaties, conventions and agreements were entered into in the 19th and 20th centuries to formalize these arrangements with varying degrees of acceptance and recognition. Over time, a 12 nautical mile territorial limit became ‘accepted’ international convention, with a right for foreign ships (including foreign war ships) to “peaceful transit”.

But this hodge-podge of legal claims and asserted rights posed a high risk of clashes or outright war on the high seas.

¹ Full text of the *Caspian Sea Convention* is available in English at <http://en.kremlin.ru/supplement/5328>

The U.N. Convention on the Law of the Sea (UNCLOS III)

In 1982, following decades of negotiations, a comprehensive accord on the rights of all nations to use the world's oceans was brokered by the United Nations. In summary, *The United Nations Convention on the Law of the Sea (UNCLOS)* codifies the customary international law of the seas. The UN Law of the Sea declares that:

- the high seas are open to all states, coastal or land-locked, that no state can claim sovereignty over any part of the high seas;
- all states enjoy freedom of navigation and overflight, the freedom to lay submarine cables and pipelines, subject to certain responsibilities ;
- all states have the freedom to construct artificial islands and other installations (i.e. oil rigs, pipelines) and the freedom of fishing, subject to conditions;
- warships on the high seas have complete immunity from the jurisdiction of any state and violation of this immunity constitutes an act of war;
- the high seas shall be reserved for peaceful purposes;
- each littoral state shall have a 12 nautical mile territorial limit extending from its coast line and a further 12 nautical miles over which the state has the right to enforce certain laws (i.e. customs, taxation, immigration and environmental protection) ;
- each littoral state has an exclusive economic zone ("EEZ") extending 200 nautical miles from its coast.

Unfortunately, UN Law of the Sea offers no definition of the high seas, only definitions of what they are not. Article 86 states that high seas include "all parts of the sea that are not included in the exclusive economic zone, in the territorial sea or in the internal waters of a state, or in the archipelagic waters of an archipelagic state".

Article 123 paradoxically creates a definition of "*semi-enclosed seas*" and then cedes jurisdiction over them to the adjacent littoral states. But the treaty goes on to define an "enclosed or semi-enclosed sea" as, in somewhat confusing language, a "sea surrounded by two or more States and connected to another sea or the ocean by a narrow outlet or consisting entirely or primarily of the territorial seas and exclusive economic zones of two or more coastal States".

The treaty does not clarify if a body of water can simultaneously be a semi-enclosed body of water and "high seas" and, if it can both at the same time, the legal consequences. Nor does the treaty define what a "narrow outlet" means – is it a natural occurring geographic feature or, as with Caspian's connection to the Black Sea, a system of canals and rivers?

Is the Caspian a "Sea" and Why it Matters

The status and rights to the Caspian turns on the question

of whether the Caspian is a "sea" or a form of "inland lake". The Caspian, while vast, saline and commonly referred to as a "sea" is not, like other seas, connected to the world's

oceans through natural waterways. If the Caspian were considered a sea, then diplomatic convention, historical legal precedents, and the UN Law of the Sea would go far to defining what international rights and obligations exist.

However, if the Caspian is determined to be an inland "lake", then international law and the UN Law of the Sea do not apply and the surrounding states would need to agree amongst themselves the extent of their territorial and resource rights. Unfortunately, there is no body under the UN Law of the Sea or elsewhere to make a binding determination.

Imperial Russia, the USSR and the Russian Federation have always considered the Caspian **not** to be an international body of water that would extend the customary rights of navigation and transit to other great powers over its surface and airspace. Russia has consistently maintained that the Caspian must be considered an inland body of water and therefore an exclusive territorial zone of the littoral states with no rights for third party ships or aircraft to transit this zone.

Iran, with the shortest coastline with relatively deep and resource-poor adjacent waters, has long maintained that Caspian is a shared lake to which each of the coastal states have joint sovereignty, rights of navigation, and a right to an equal share in all oil and gas resources (before the dissolution of the USSR, on a 50/50 basis and after, 20% to each of the 5 littoral states).

In 1921 and 1940 the USSR and Iran entered into treaties to agree that the Caspian Sea is not an international body of water. Each agreed to treat the body of water as a "condominium" having an undivided 50% share of the Caspian.

In addition, Iran has not ratified the UN Law of the Sea (nor has the United States). It is surmised that this is because Tehran wants to keep its territorial claims to the Persian Gulf, and in particular, its claimed right to control passage of oil tankers through the strategically important Straits of Hormuz .

Pipeline Diplomacy

In recent decades the Russian Federation, wanting to maintain its chokehold on gas exports from the North Caspian to Europe, has intentionally remained ambiguous on the status of the Caspian, thus making construction of pipelines from Kazakhstan or Turkmenistan to the west impossible.

In the north, Russia, and in the south, Iran, have their own pipelines to transport oil and gas to market. Azerbaijan, on the western shore of the Caspian, via the Southern Gas Project, transports gas through Georgia into Turkey and onto the Mediterranean. But while the status of seabed rights remain outstanding, Turkmenistan cannot build the proposed 300km “Trans-Caspian Pipeline” under the Caspian to the shores of Azerbaijan to link-up with the Southern Gas corridor to Europe.



The Caspian Sea Compromise

On the 12th August 2018, after more than 20 years of on-again off-again talks, the five littoral powers finally made a breakthrough on trade, security, and the environment. The Caspian Sea Convention defines the legal status of the surface waters, the seabed, natural resources, and subsoil rights. It establishes sovereign and exclusive rights for each of the coastal States in their respective territorial waters and seabed and subsoil sectors. The accord limits third party military forces from the use of the waters or airspace.

The waters of the Caspian Sea are divided into three zones: territorial waters, fishery zones and the “common maritime space”. The territorial waters extend from the coastal baseline out 15 nautical miles. The respective fishery zones extend a further 10 nautical miles adjacent to the territorial waters, in which each state has exclusive rights over the aquatic biological resources. The Convention specifies that the exact delimitation of territorial waters and fishery zones between the respective states is to be determined by further agreement with regard to the “principles and norms” of international law. No such delimitation agreement has been concluded so far between the coastal states.

The waters located beyond the parties’ respective fishery zones (25 nautical miles) are part of the “common maritime space” which is open for the navigation and use by each of the states, but to the exclusion of other states.

Why Now? – The Exclusion of Foreign Military Forces?

It seems that Russia and Iran have agreed to compromise their economic claims over the Caspian in order to bolster their regional security.

Russia has long sought to re-establish its exclusive military dominance on the Caspian as it did in 1813 under the *Treaty of Gulistan* between Iran and Russia. Under that treaty the two countries agreed that the Russian Navy was the only military force permitted on the Caspian².

Under the Caspian Convention Article 3(6) the deployment of any military forces or vessels not belonging to a signatory party is prohibited. Article 3(7) prohibits a signatory from allowing use of any part of its territory by other states to commit acts of aggression or undertake other military

actions against a signatory. Article 3(8) allows the ships of each of the five nations, including its naval ships, to navigate anywhere in the Caspian outside the territorial zones.

This, in effect, cedes military control of the Caspian to the Russian Navy. Russia had always opposed alternative solutions based on national coastlines that would have limited Russia’s military presence to the northwest of the Caspian.

Iran, increasing isolated and under pressure from the United States, decided that the benefits of being aligned with Russia as well excluding US military and NATO forces from the Caspian was worth surrendering its claim to a full 20% of all resources in the Caspian. Notwithstanding the security benefits to Iran, the agreement has been criticized in Iran as a surrender of territorial rights. Tehran was the last of the 5 parties to agree to the terms of the treaty and only at the 11th hour before the signing in Aktau. It can be expected that Tehran will be slow to ratify the treaty – if ever.

The Future of Caspian Pipelines

The Caspian Sea Convention addresses the right of five states to construct sub-sea pipelines on the sea-bed. Article 14 of the Convention states that the parties “... may lay submarine cables and pipelines on the bed” and goes on to state that “submarine cables and pipelines routes shall be determined by agreement with the Party the seabed sector of which is to be crossed by the cable or pipeline.”

² *The Treaty of Gulistan signed by Persia and Russia on 24 October, 1813 after the Russo-Iranian wars granted Russia right to have only its navy in the Caspian Sea, the right of both contracting parties’ merchants to trade freely over the Caspian, and delimited for the first time the border between both countries on the basis of the status quo ad praesentium principle*

In the case of the Trans Caspian Pipeline this would mean that only Turkmenistan and Azerbaijan need to agree on the route.

While this provision would appear to “green light” construction of the Trans-Caspian Pipeline, it is not “clear blue water” for Turkmenistan. The treaty has extensive environmental protections. Russia has long-standing objections to the Trans-Caspian Pipeline on the basis (spurious or not) of the potential harm to the Caspian if the pipeline were to be constructed.



Environmental Protections – Tehran Convention

The Caspian Sea Convention states that sub-sea projects must “comply with environmental standards and requirements embodied in the international agreements to which they are parties”. It also requires that the five states protect the ecological system and biodiversity of the Caspian Sea, take necessary measures to ensure such protection, and to prohibit any activity damaging the biodiversity of the Caspian Sea. These obligations must be taken into account for the future development its hydrocarbon resources.

In 2003 the five Caspian states agreed to the Tehran Convention³ with the objective of “protection of the Caspian environment from all sources of pollution including the protection, preservation, restoration and sustainable and rational use of the biological resources of the Caspian Sea”. Under the Tehran Convention the following additional protocols apply to any activity:

- *The Protocol on Conservation of Biological Diversity* (the “**Ashgabat Protocol**”)⁴;

³ *The Framework Convention for the Protection of the Marine Environment of the Caspian Sea was signed by Azerbaijan, Iran, Kazakhstan, Russian Federation and Turkmenistan in Tehran on 4 November 2003 and entered into force on 12 August 2006.*

⁴ *The Ashgabat Protocol was adopted and signed at the fifth Meeting of the Tehran Conference (COP5) in Ashgabat, Turkmenistan, on 30 May 2014.*

- *The Protocol for the Protection of the Caspian Sea against Pollution from Land based Sources and Activities* (the “**Moscow Protocol**”)⁵;
- *the Protocol Concerning Regional Preparedness, Response and Cooperation in Combating Oil Pollution Incidents* (the “**Aktau Protocol**”)⁶; and
- *the Protocol on Environment Impact Assessment in a Transboundary Context*⁷.

These environmental protocols impose an obligation to notify, exchange information and consult with all 5 states on all projects. As a result this has the potential to stall the Trans-Caspian Pipeline and other projects for a long period.

It has been suggested that each of the five littoral states have the right **only** to give an opinion on a project and this must be done within a 6-month window. This consultation does not grant each state an absolute right of veto. Nevertheless, there are significant legal and diplomatic hurdles to be surmounted with any project in the Caspian – particular those which by-pass Russian and Iranian pipelines.

Conclusion

From an economic stand-point, Kazakhstan, Turkmenistan and Azerbaijan are the clear winners from the Caspian Sea Convention. It will allow each state to develop additional off-shore oil and gas fields and opens the possibility of these states building sub-sea pipe-lines to access western markets.

Russia and Iran have achieved their security objective by preventing the Caspian Sea and the airspace above from being used by any outside military force (i.e. NATO or the United States).

In addition, from the perspective of Russia and Gazprom, the convention cannot be considered a clear “green light” for Turkmenistan to construct the Trans-Caspian Pipeline. Russia has not withdrawn its objections, on what seems to be spurious environmental grounds, to the construction of this sub-sea pipeline.

Finally, the Caspian Sea Convention must be ratified by all five countries before it comes into effect. The timing for ratification, particularly by Iran, is anyone’s guess. The “Great Game” continues.

⁵ *The Moscow Protocol was adopted and signed at the fourth Meeting of the Tehran Conference (COP4) in Moscow, December 12, 2012*

⁶ *The Aktau Protocol was adopted and signed at the third Meeting of the Tehran Conference (COP3) in Aktau, August 12, 2011*

⁷ *Adopted and signed at the Extraordinary Meeting of the Tehran Conference in Moscow, July 20, 2018*

RECLAIMING LOST ASSETS FROM DEBTORS IN BANKRUPTCY COURT

Alibi Akylas, Legal Consultant
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Creditors may face a situation in which the creditor's organization is owed money, yet the debtor has filed for bankruptcy. If the court upholds the petition, the debtor faces bankruptcy procedures and the court will free him or her from unpaid debts. It is important to the creditor to consider what steps should be taken to avoid losing the original investment.

In any bankruptcy case, it is imperative that both parties act quickly. The debtor's main aim is to free himself of debts by removing remaining assets from his company as quickly as possible, whereas the creditor's goal is to regain as much of his investment as possible.

Filing a Proof of Claim

To ensure recovery of lost assets, the creditor must file a proof of claim with a temporary administrator within the allotted time. Unfortunately, the creditor has only one month to file, otherwise he will be treated as a *non-voting* creditor, which essentially gives him no influence over the bankruptcy proceedings.

Furthermore, creditors who miss the deadline will only get a chance to recover their lost investment after creditors who register their claims on time. Therefore, missing this deadline may force the creditor to wait until the very end of bankruptcy proceedings to make his case. In a recent court case, a major creditor with a claim in excess of 500 million Tenge missed the filing deadline. Taking advantage of this, the debtor arranged to exclude his assets from the proceedings to protect them from liquidation. After disputing the temporary bankruptcy administrator's actions, the decision was overruled.

In another case, a major creditor had a claim to a debtor for one billion Tenge. However, this creditor also missed the temporary administrator's deadline and was forced to abstain from the proceedings. This played into the hands of the debtor, who was waiting for the statute of limitation to end on his most valued asset: a subsoil use contract. While the creditor's party wanted to liquidate the asset, they had no legal authority to do so.



The Bankrupt Entity's Financial Condition

In these situations, creditors should study a debtor's financial condition. By law, bankruptcy petitions should include a debtor's financial statements for the past three years and list all of their assets and debts. Creditors should take advantage of this by reviewing all the debtor's financial documents.

The creditor does not have to limit himself to studying published documents but may also try to find additional information from open sources and review the petition itself, which should list the reasons for the company's insolvency.

In one court case, Deloitte managed to locate and compare a debtor's financial statements with the published audit report, from which it soon became clear that there were discrepancies in the figures amounting to hundreds of millions of Tenge. It turns out that the figures had been altered in the financial statements so that the court would be more inclined to award the case to the debtor. Eventually, the court considered these facts and upheld the creditors' position.

It is therefore in the creditor's interest to identify the cause of bankruptcy by analyzing the available financial documents.

Generally speaking, bankruptcy takes one of three forms (i) *accidental*, (ii) *negligent* (iii) or *intentional*. Recovering assets from an accidental bankruptcy is extremely difficult, but creditors typically have more success in cases of negligence and intentional bankruptcy.

Suspicious Debtor Transactions and Operations

Most debtors, irrespective of the reasons for their bankruptcy, want to strip their companies of all remaining assets rather than liquidate them. These debtors have a number of methods at their disposal, but a transaction or arrangement of some kind is always involved. Here are some examples:

- *Assets are sold at low prices prior to bankruptcy to "friendly" companies, which are subsequently liquidated, meaning there is nobody left to petition;*
- *A controllable debt is created, after which a "friendly" creditor petitions a court, receives its ruling and, through execution proceedings, strips the debtor's assets;*
- *A valuable asset is stripped through corporate reorganization, creating a new company from the bankrupt company and acquiring all its assets, leaving the debtor with nothing.*

A creditor and bankruptcy administrator's goal is to discover any such transactions and return assets to debtors so they can be allocated to creditors. Any creditor discovering an unusual transaction can report findings to the bankruptcy administrator, who should then ask the court to have the transaction declared invalid. If the court rules in the bankruptcy administrator's favor, the asset is returned to the debtor's balance sheet.

In one instance a debtor, before filing for bankruptcy, significantly increased company management salaries to approximately 70 million Tenge, which, over the period of a few months, managed to cover amounts due to other creditors. The debtor's goal was to strip assets because salary arrears are considered a priority for creditors.

Joint Company Management

Furthermore, if a company is declared bankrupt, management may be made jointly liable for any outstanding company debts. For example, if a company owes 100 million Tenge, but it only has assets worth 10 million, then,

if there are grounds, management may be made liable for the remaining 90 million.

Grounds in these cases usually include:

- *A debtor's failure to petition a court for bankruptcy within six months of the day it became aware or should have become aware of its insolvency;*
- *A debtor upholding a creditor's claims, which makes it impossible for him to repay cash liabilities to other creditors;*
- *Management's intentional actions to bankrupt their company.*

With proper research and counsel, companies can greatly increase their chances of reclaiming debts owed to them. However, it is worth noting that situations do arise when it is not advisable to wait for a debtor to declare bankruptcy. In these instances, creditors should initiate legal proceedings first if they feel their assets are at risk.

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KAZAKHSTAN'S NEW CURRENCY LAW

**Gulnur Bekmukhanbetova, Senior Associate
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Kazakhstan is well known for having a liberal currency system, a key factor in the nation's success in attracting foreign investment. However, on July 2, 2018, a new currency law¹ was adopted in Kazakhstan that will replace the 2005 currency law², effective July 1, 2019. The new currency law significantly changes the country's existing currency regulations.

According to various materials prepared by the National Bank of Kazakhstan (NBK)³, the new currency law is intended to improve *statistical monitoring of foreign exchange transactions* and, furthermore, is needed in light of Kazakhstan's accession to the WTO to *adapt the legislative framework in the field of currency regulation to new economic conditions*. However, the main effect of the new currency law is to limit foreign currency transactions and to expand the use of local currency, the Tenge, which has been depreciating since 2009.

This article considers certain legal and practical issues for foreign investors operating in Kazakhstan following introduction of the new currency law.



New Definition of 'Currency Resident'

Perhaps the most controversial provision in the new currency law is its change of status for branches and representative offices of foreign companies from *non-currency resident* to 'currency resident'. The general rule

¹ Law On Currency Regulation and Currency Control dated 2 July 2018, No. 167-VI ZRK (the "New Currency Law")

² Law On Currency Regulation and Currency Control dated 13 June 2005 No. 57-III ZRK, as amended, (the "Existing Currency Law")

³ See the NBK Concept of the Draft Law On Currency Regulation and Currency Control and Explanatory Note from the Government to the Majilis to accompany the Draft dated 28 December 2017.

under both the existing currency law and new currency law is that non-currency residents may transact operations with residents in foreign currency. The definition of non-currency residents in the existing currency law includes branches and representative offices of foreign companies. However, under the new law, branches and representative offices of foreign non-financial organizations⁴ are deemed to be residents if they create a permanent establishment (PE) in Kazakhstan for tax purposes.

As a result, most foreign branches (and representative offices) will no longer be able to transact with their local counterparties in foreign currency and will be required to use Tenge, since such branches (and representative offices) are now treated as residents. This is a very serious (and potentially expensive) change for many foreign companies operating under the branch (representative office) model in Kazakhstan.

The definition of residents in the new currency law refers to branches and representative offices *which create a permanent establishment ... in the Republic of Kazakhstan in accordance with the [Tax Code] of the Republic of Kazakhstan*. Branches are automatically PEs under the Tax Code. However, representative offices are non-commercial units of their parent companies and, as such, do not normally create a PE. This means that some, but not all, representative offices will be treated as currency residents, depending on whether a particular representative office is determined to act through a PE.

However, it is unclear who will make such determination in practice and when such a decision will be made. This may create serious issues in practice for representative offices when they attempt to make bank transfers in foreign currency as local banks may insist on evidence that they are not carrying out activities through a PE.

Exception for Subsoil Company Branches

With respect to branches of major subsoil companies, the new currency law provides an exception and states that certain branches will continue to be considered non-currency residents. A list of such branches (and representative offices) will be established by the Kazakh government.

⁴ With respect to financial organizations, foreign banks and insurance firms are prohibited from carrying out activities through a branch in Kazakhstan, thus there are no current branches of foreign financial organizations.

In December 2020, foreign banks and insurance firms will be allowed to carry out activities through a branch, in which case such branches will be treated, for currency purposes, as "residents."

This exception is intended to primarily cover subsoil (oil, gas, and mining) companies operating as branches in Kazakhstan under profit-sharing agreements or other subsoil use agreements with the government, provided that such agreements expressly indicate that such branches are non-currency residents. The NBK is currently working on the list of exempt branches based on copies of agreements with the government provided subsoil companies.

This exception in the new currency law is limited to subsoil company branches contained in the government's list and does not extend to their sub-contractors who also operate as branches and deal extensively with residents. Thus, even though the branches of sub-contractors will be able to transact in foreign currency with the listed branches of subsoil companies, they will need to use Tenge for their transactions with other local counterparties.

Exception for Certain Transactions

As with the existing currency law, the new currency law permits foreign currency transactions between residents and non-currency residents.

In addition, the new currency law provides that the following additional types of transactions involving branches (or representative offices) (which the new currency law considers to be residents) are exempt from the requirement to use Tenge and therefore may be carried out in foreign currency:

- (i) *transactions between branches (or representative offices) of different foreign companies;*
- (ii) *transactions between a branch (or representative office) and its home office outside of Kazakhstan.*

However, it is unclear how the exception referred to in (ii) above will work in practice since a branch (representative office) cannot enter into transactions on its own because it is inseparable from its home office.

Payment of Salaries in Foreign Currency

The existing currency law specifically permits non-currency residents to pay salaries to their employees in any currency. The new currency law omits such a right (although it does not expressly prohibit salary payments in foreign currency), notwithstanding that the right to pay employees, particularly many highly-skilled foreign employees, in foreign currency is critical for foreign companies in Kazakhstan.

The NBK has indicated that this change is intended to bring the currency legislation in line with the labor code, which require all salary payments made in Kazakhstan to be in Tenge. All employers in Kazakhstan (including branches

(representative offices) of subsoil companies that will be on the government's list of non-currency residents under the new currency law) are subject to the labor code's provision requiring salary payments made in Kazakhstan to be in Tenge.



New Disclosure Requirement

The new currency law introduces a new term for *operations aimed at withdrawal of funds from Kazakhstan*. Such operations include the following:

- (i) *a financial loan from a non-resident to a resident where the loan proceeds are credited to the resident's foreign bank accounts, bypassing local accounts opened with Kazakhstani banks;*
- (ii) *a financial loan from a resident to a non-resident where the repayment of the loan is made to the resident's foreign bank accounts bypassing local accounts opened with Kazakhstani banks;*
- (iii) *an interest-free loan from a resident to an unaffiliated non-resident for a term exceeding 720 days;*
- (iv) *export/import operations involving a delay in delivery of the non-resident's payments obligations for more than 720 days after the date when the resident fulfills its obligations.*

Local servicing banks are prohibited from processing payments under any of the above transactions without the specific written consent of the resident party authorizing the servicing bank to disclose information on the transaction to the NBK. Although the disclosure is required, the NBK cannot stop or suspend the reported transaction under the new currency law.

The disclosure requirement does not apply to branches and representative offices of foreign companies (including subsoil companies) as well as to financial loans made under trade and Islamic financing operations.

The NBK Interpretation Letter

The new currency law is unclear on whether it applies to existing agreements for foreign branches made prior to July 1, 2019. In response to Baker McKenzie's interpretation request, the NBK issued a letter to Baker McKenzie dated October 5, 2018 in which it confirmed that the new currency law has no retroactive effect and therefore should not apply to existing agreements of foreign branches (representative offices) signed prior to July 1, 2019.

However, if such an existing agreement is amended at any time after July 1, 2019 by way of an assignment of the agreement to a branch (representative office) of another foreign company, the stability of the agreement will be lost and the new currency law will take precedence over such agreement (as assigned to the new party).

The NBK also confirmed in its letter that branches of EU companies in existence as of July 2, 2018 (when the new currency law was adopted) should be able to apply the three-year grace period provided under the 1995 *Kazakhstan-EU Agreement*⁵, and therefore the new law

⁵ *Kazakhstan-EU Partnership and Cooperation Agreement dated 23 January 1995 (the Kazakhstan-EU Agreement).*

should not apply to agreements with branches of EU companies made prior to July 2, 2021. Under the 1995 *Kazakhstan-EU Agreement*, where new legislation would render operating conditions of branches (and subsidiaries) of EU companies more restrictive, such legislation shall not apply for three years following the entry into force of the law to those branches (and subsidiaries). While not addressed in the NBK interpretation letter, we believe that the three-year grace period for branches of EU companies generally should extend to branches of companies from other countries (including the U.S. and Japan) based upon the most favored nation provisions contained in their bilateral investment treaties with Kazakhstan.

Conclusion

The changes to Kazakhstan's existing currency system contained in the new currency law will make it more challenging and expensive for foreign investors to conduct business in Kazakhstan, particularly those operating through a branch or representative office. This will likely affect Kazakhstan's reputation for having liberal currency policies. Foreign companies may consider reviewing their existing structures and their arrangements with counterparties to prepare themselves for the new currency regulations and to understand what can be done to mitigate the risks arising from the new legislation.

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AMENDMENTS TO KAZAKHSTAN'S IP LEGISLATION

Andrei Yorsh, Partner
Baker McKenzie

On July 6, 2018, amendments to the law *On Trademarks, Service Marks, and Appellations of Origin* (the Law) entered into force in Kazakhstan.

The amendments to this law affect a wide range of issues, including powers of the Ministry of Justice as an authorized body to protect intellectual property rights, powers of the *National Intellectual Property Institute* as an expert organization, the procedure for trademark registration, service marks and appellations of origin, the procedure for recognition of trademarks as well known, for transfer of trademark rights, for challenging trademark registrations, the scope of protection of trademark rights, and the status of patent attorneys.



In general, several of the changes should simplify trademark registration procedures. However, several provisions related to IP protection in Kazakhstan may affect the level of protection for trademarks and appellations of origin. For example, the term *exhaustion* of exclusive trademark rights is introduced in the Law. Despite the existence of a previous rule, the lack of a term in the past gave rise to disputes over the legitimacy of the use of trademarks for goods imported from Eurasian Economic Union member states. With the new term, legislative agencies have eliminated this gap.

In addition, the concept of *counterfeit goods*, previously absent from the legislation, is expressly introduced in the Law. Goods are recognized to be counterfeit if trademarks, appellations of origin, or confusingly similar designations are placed on such goods and their packaging without the legitimate trademark owner's consent.

The new version of the Law provides that only counterfeit goods are now subject to removal from the market and destruction. This means that original goods that were placed on the market in breach of the trademark owner's rights (parallel import) are not subject to seizure or destruction.



In certain instances under the Law, counterfeit goods and their packaging can nonetheless be placed on sale if this is deemed to be in the public interest and does not breach Kazakhstani consumer protection legislation. Thus, Kazakhstan is moving towards legalizing sale of counterfeit goods, a questionable and undesirable practice.

Another change in the Law is granting to trademark owners the right to claim *compensation* instead of damages (so-called *alternative liability*) from trademark rights' infringers. The amount of compensation will be determined by the court based on the nature of the breach and the market value of the homogeneous/original goods on which a trademark, appellation of name origin, or confusingly similar designation has been placed with the owner's consent. The local courts have not yet tested this provision, so how the courts will implement and enforce it is not yet known.



ENFORCING FOREIGN ARBITRAL AWARDS IN KAZAKHSTAN

Duman Akhmetov, Partner
INTEGRITES International Law Firm

The article below discusses enforcement of foreign arbitral awards against local resident defendants.

Many Kazakhstani companies are increasingly working with foreign businesses. As a result, when negotiating a contract, foreign partners often suggest choosing foreign arbitration as an independent forum for resolving potential disputes between all parties to the transaction. Enforcing these arbitration awards in Kazakhstan can often be a challenging process, but INTEGRITES has had success navigating these procedures.

Arbitration proceedings are regulated by the *United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards (New York Convention)*. According to the *United Nations Commission on International Trade Law (UNCITRAL)*, 159 countries are currently parties to this convention. The New York Convention obliges signatory states to recognize and enforce foreign arbitral awards on their territory, which Kazakhstan agreed to do when it acceded to the Convention in 1995 without reservation.

The New York Convention provides an exhaustive list of grounds outlining the conditions under which a country may refuse enforcement of a foreign arbitral award on its territory. However, *Kazakhstan's Civil Procedure Code No. 377-V* also envisages an additional procedure for enforcing these awards, under which local courts must first review an arbitral award and only then issue an enforcement order.

Although this would seem a simple, straightforward process, in reality it creates many legal obstacles when enforcing such awards. In our firm's experience, challenges often arise when local courts inadequately interpret and apply these procedural rules.

Courts often abuse their authority by assessing the legal validity of a foreign arbitral award, which is a violation of the law. Courts may indicate a lack of evidence in a case or state that the debtor has presented new evidence affecting the foreign arbitral award. Despite the legality associated with such actions, courts have demonstrated various types of abuse over the years.

There are other challenges concerning the broad interpretation of documents required for recognizing and enforcing foreign arbitral awards. The *Civil Procedure Code and Regulatory Resolution of Kazakhstan's Supreme Court No. 5* require an exhaustive list of documents for these proceedings. In practice, local courts even require submitting additional documents about the merits of the dispute and other regulatory issues.

More difficulties arise when the courts require additional legalization requirements for documents attached to arbitration enforcement applications. Documents issued, compiled or, certified by competent foreign authorities outside Kazakhstan should be accepted by Kazakhstani courts if they have consular legalization, unless otherwise stated.

However, in practice judges often require foreign legal documents to be further legalized by a local body, despite the fact that Kazakhstan and the issuing country are both parties to the *Hague Convention*. Sometimes judges require the documents to be apostilled, even though Kazakhstan is a party to international mutual recognition agreements that make this unnecessary.

To complicate matters further, despite the fact that Kazakhstani procedural rules state it is sufficient to provide a certified copy of a foreign arbitral award, local courts often demand the original document as well.

After eliminating all obstacles in Kazakhstan's local courts, the applicant may encounter further problems enforcing the arbitral award. Bailiffs will typically enforce an arbitral award immediately upon issuance of an order by a local court. However, enforcement can sometimes be ruled illegal by a different local court as the result of the defendant's claim. There will thus be two conflicting judicial decisions in effect, namely: determination by one court to recognize and enforce an award, and a decision by another court declaring the bailiff's actions unlawful.

Although the legal procedure for obtaining an enforcement order in Kazakhstan is quite straightforward, there are often huge obstacles associated with the inadequate interpretation and application of international agreements and norms. Integrates law firm has successfully enforced foreign arbitral awards in these circumstances by appealing to higher authorities or initiating enforcement proceedings with another bailiff.

Overall, potential investors should be aware of the issues affecting foreign arbitral awards when planning joint business with local partners. Not all judges correctly apply the norms of international agreements and procedural legislation, therefore leading to unlawful refusals, loss of time, and legal costs. It is recommended to seek legal advice beforehand and request additional documents before sending the award to Kazakh courts.

The effectiveness of any enforcement also depends on the bailiff. It is necessary to work closely with the bailiff to reduce any omissions, whenever possible. These preventative actions can help foreign clients save time and money, and will protect their businesses from future legal problems.

FIVE KEY M&A TRENDS IN KAZAKHSTAN TODAY

by Liza Zhumakhmetova, Partner, SIGNUM Law
Rustam Baitazin, Associate, SIGNUM Law

Allen & Overy recently published a survey of the global M&A market for the first quarter of 2018. The survey states that, despite continuing geo-political uncertainty, the global M&A market is now enjoying the longest cycle of growth ever recorded. Key regions are powering ahead and mega-deals are back on the agenda in many sectors, indicating an extraordinary level of confidence among investors¹.

In light of the global transactions market remarkable growth, we would like to highlight five major trends we have witnessed in recent years in Kazakhstan's M&A market. Our insights are based on recent experience supporting domestic and multi-jurisdiction M&A deals in Kazakhstan.



Pharmaceuticals

Despite the downturn in overall global market deal value, the pharmaceutical sector continues to deliver large, industry-shifting transactions. M&A in this sector has been generally driven by the need for large pharma groups to refill their product pipelines and move into new treatment areas. Among recent major international deals are Takeda's \$76 billion acquisition of Shire, which dominates the numbers, and Sanofi's \$11.1 billion acquisition of Bioverativ².

While the global pharmaceutical players such as Sanofi, GlaxoSmithKline, Teva, Takeda, Pfizer and others are continuing to expand their business operations in Kazakhstan, strong domestic players are now in a position to compete for customers. Increasing competition in the near term may lead to the necessity for local players to pool efforts through consolidation and merger of their businesses.

Renewable Energy

The world is looking for a transition from traditional energy resources to renewable energy resources. Today, the global "energy pie" consists of 87% carbon-based fuels and only 13% alternative energy. Kazakhstan urgently needs to develop and implement a set of measures and

policies for renewable energy. The first steps in this direction took place at the EXPO-2017 International Exhibition in Astana. This exhibition gave a major push to international investment in Kazakhstan's renewable energy sector.

Recent key acquisitions in the industry took place in Kazakhstan's eastern and southern regions, but for the time being Chinese and European investors are champions among investors interested in this sector. In light of a number of deals which our M&A practice supported in the last two years, we will likely see more renewable energy transactions in the months ahead. This is good news indeed for the development of alternative energy and a cleaner environment in Kazakhstan!

Privatization – In Process with More to Come

The national privatization program for 2016-2020, involving more than 877 entities, is 76 percent complete with 397 organizations worth 199 billion Tenge (\$619 million.) sold and 274 entities set for reorganization and liquidation, according to Minister of Finance Bakhyt Sultanov³. We have seen a keen interest from Chinese investors for scientific research institutions as part of the privatization program.

We further expect to see more large-scale M&A transactions allowing local and international players access to major strategic Kazakh assets, which have been traditionally (historically) reserved for state ownership.

Up next for privatization on the AIFC Stock Exchange⁴ are some of Kazakhstan's largest state-owned companies like *Kazakhstan Temir Zholy* (Kazakh railways), *KazMunaiGaz*, *Kazatomprom*, *Samruk-Energy*, *Tau-Ken Samruk* mining, *Kazpost*, and *Air Astana*.

One Belt, One Road

Another key driver that may boost the economy in the near future is China's *One Belt, One Road* initiative, the trade and development strategy unveiled by President Jinping Xi in September 2013, which aims to improve trade relations between China and the Western world. It is no secret that Kazakhstan must and will benefit from this initiative due to its location in the heart of the Eurasian belt and openness to actively work with all players.

The *One Belt One Road* initiative is already well underway, and the Chinese government announced that it has signed 100 cooperation agreements with 86 countries and international organizations. In December 2015, the governments of Kazakhstan and China signed investment agreements worth \$14 billion.

1 Allen & Overy, *Long Distance Running, M&A Insights H1 2018*

2 Ibid

3 <https://kapital.kz/finance/bakhyt-sultanov-nazval-chastye-narusheniya-pri-privatizacii.html>

4 <http://privatization.gosreestr.kz/>

The major areas for Chinese investments in our economy are in the banking and agro-industrial sectors. For instance, the Bank of China and ICBC are already operating within the Astana International Financial Center (AIFC) and Chinese investors plan to build an agro-industrial complex in Southern Kazakhstan worth \$100 million.



Acquisitions of Shell Companies

A recent trend in small/mid-level transactions shows how foreign investors choose to enter the Kazakh market. Considering the significant level of state regulatory control in some areas of the national economy, coupled with difficult and time-consuming licensing/permission procedures, the acquisition of shell companies appears to be an excellent option.

The concept of a so-called shell company in the Kazakhstani context relates to companies that hold a certain license/permit, but have a dormant status at the time of its acquisition. While the direct/indirect acquisition of a shell company by a foreign company is a legitimate way to acquire a business in general, as it reduces costs and saves time in dealing with all the regulatory procedures and approvals (which can be a nightmare), one should be cautious of the risks associated with these businesses, commercial, legal or otherwise. It is essential for a foreign investor to conduct due diligence of the shell company and assess all the pros and cons of this an option.

Our firm has recently supported numerous acquisitions by European and Chinese companies of shell companies with category one construction licenses and category one licenses for mining operations. In these situations, it is important to ensure that there is no imminent risk of license revocation or suspension due to prior dormancy status. It is also imperative that all requirements and licensing terms are met and followed.

Overall, the future is hopeful, and we believe the trends described above may provide insight for readers seeking indications for domestic and global economic growth.



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AMCHAM ANNUAL GENERAL MEETING 2018 ANNUAL REPORT TO MEMBERS

The AmCham Annual General Meeting (AGM) at which Board Members report each year on AmCham's achievements of the previous year, was held at the Rixos Almaty Hotel on Friday evening, 1 February 2019. Speaking to a capacity audience in the Lotus Restaurant, Canadian Ambassador Nicholas Brousseau, one of AmCham's strongest supporters in the international diplomatic community, welcomed AmCham members and spoke about AmCham's outstanding advocacy work with the Government of Kazakhstan and AmCham's development in Kazakhstan over the past decade.



Canadian Ambassador Nicholas Brousseau

2018 AmCham Advocacy: AmCham Executive Director Doris Bradbury then took the podium to report more fully on AmCham Advocacy over the past year, as well as outlining the history of the AmCham dialogue platform with the Government of Kazakhstan, the *Council to Improve the Investment Environment*. The Council, which was created ten years ago exclusively for AmCham and its members, is chaired each month by the Prime Minister and a panel of Cabinet Ministers responsible for the country's economy and justice system.

The Council brings together an official panel of ten AmCham CEOs that rotate annually, along with speakers from AmCham member companies, ambassadors, and invited guests from international institutions such as the OECD, EBRD, IFC, IMF, ADB, WB, IDB, and WHO. AmCham chooses each month's topics, and 2018 Council topics included *New Initiatives in Judicial Reform*, *Challenges to Economic Diversification*, *Healthcare Reform and the New Health Code*, *Creating a Level Playing Field for Investors: Competition vs. Discrimination*, *AmCham Member Award-Winning CSR Projects*, and environmental topics involving the oil industry and renewable energy.

Challenges to Economic Diversification was expanded into a full-day conference open to the investment community, diplomatic community, international organizations, NGOs,

and the Government. As always, the AmCham conferences are opened by prominent Keynote Speakers. This year's conference in Astana was opened by *Deputy Prime Minister and Agriculture Minister Umirzak Shukeyev*, *U.S. Ambassador George Krol*, and *Canadian Ambassador Nicholas Brousseau*.

The *Competition vs Discrimination* topic produced strong support from the Prime Minister, who requested that AmCham seek foreign experts who could spearhead reform of the fair competition and anti-monopoly legislation. AmCham turned to the OECD, which had delivered a key presentation at the Council on this topic, and an OECD program was developed and delivered to the Prime Minister for consideration. If the program is implemented with strong support from the Prime Minister, it will have a very positive impact on Kazakhstan's investment climate.



AmCham Executive Director Doris Bradbury

The *Healthcare* topic was motivated by the Health Ministry's year-long efforts to reform the Health Code, and resulted in the two Chairs of AmCham's Healthcare Reform Working Group and Intellectual Property Working Group, participating in drafting the new Health Code. AmCham consultations with the World Health Organization (WHO) helped to inform both the Council discussions with Health Minister Birtanov and recommendations for the new Code.

The Prime Minister responded positively to Council presentations of a variety of corporate social responsibility projects in the fields of health, labor, agriculture, refugee support, and culture. He noted that he generally does not hear about the social projects designed, funded, and implemented by the investment community, and wants to hear more about investor activity in addition to the commercial and trade benefits investors bring to Kazakhstan.

A full year of monthly Council topics is already underway in 2019 with *Tax Reform: Dispute Resolution vs. Litigation* as the January topic and *Cybersecurity and Cybercrime: Challenges for the 21st Century* as the February topic.

2018 AmCham Membership Trends: *Gani Uzbekov, AmCham Board Member and Founder and CEO of S1LK*, reported on Membership Trends in 2018. Starting as a small group of 36 American companies that launched AmCham in 1999, AmCham has today grown to a highly diverse organization with a membership base of over 200 companies from all corners of the globe, 75% of which are in the elite Corporate A membership category: global leaders with annual revenue in excess of \$100 million. Smaller companies have decreased in recent years, hard hit by economic stress and uncertainty due to successive global financial crises and several years of low oil prices.

The oil industry and those industry sectors servicing the industry – *oilfield services, engineering, logistics, financial and legal services* – continue to spearhead the largest segment of the AmCham membership. *Consumer products* is another leading membership sector, demonstrating the affluence of Kazakhstan's consumers purchasing foreign goods in the country's oil-based economy.

In the wake of Expo 2017 and the explosive growth of the *hospitality industry* to service Expo, hotels and travel make up an increasingly large membership sector. Also notable is the continuing growth in the *pharmaceutical sector* as Kazakhstan embarks on healthcare reform. Global pharmaceutical leaders are contributing to the reform process, enforcing intellectual property rights to protect their pharmaceutical patents.



U.S. Commercial Counsellor Dean Matlack

2018 AmCham Working Groups: *Dean Matlack, Commercial Counsellor, U.S. Consulate General Almaty* spoke about the 25 AmCham Working Groups spread across Kazakhstan. AmCham Working Groups have flourished in recent years, reaching a total of 21 Internal Working Groups plus 4 Inter-Ministerial Working Groups. These Groups meet in a total of five cities – each group focusing on topics specific to their geographic region and regional industry characteristics.

The Inter-Ministerial Working Groups are linked by video to Ministries in Astana to enable participation from AmCham members based in other major cities in Kazakhstan. The internal AmCham Working Groups also play an increasingly important role in advocacy by highlighting issues of concern, developing and submitting recommendations to the Government of Kazakhstan. The Healthcare Reform Working Group works closely with the Intellectual Property Working Group in pushing for improved pharmaceutical patent protection. Some of the Groups are duplicated in various cities, each with their own Chair, depending on member interest in different locations.



Several of the Inter-Ministerial Groups, which were created to achieve resolution to specific problems – VAT refunds, Licensing Reform – achieved their objectives to a sufficient degree to close the Groups or to transform them into Groups on related topics. For instance, the VAT Refunds Working Group was transformed into a larger Inter-Ministerial Tax Reform Working Group when the Group members felt they had achieved an adequate, if not perfect objective with a schedule of VAT refunds for the oil industry. The new Group continues to monitor VAT refunds, but also conducts advocacy for a range of other tax reforms.

2018 AmCham Regional Strategy: *Andrey Kurilin, CEO of Citibank Kazakhstan and Former AmCham Board Member*, took the podium to discuss AmCham's Regional Strategy. Beyond Almaty, AmCham has a solid presence in Kazakhstan's regional cities: Atyrau and Aktau in the Caspian region, Shymkent, the burgeoning southern city, and the country's capital, Astana. Each city has an AmCham Regional Representative who ensures that AmCham remains well-informed about events, trends, and member issues in each location. The Resident Representatives are CEOs of leading AmCham member companies who perform representative functions for AmCham whenever necessary.

AmCham organizes events in the regional cities, as well as in Almaty, effectively remaining in touch with the local membership and bringing members together in force – including with the diplomatic community during large international events in each location during the year.



AmCham Board Member Olga Voronova,
Country Manager, Procter & Gamble

2018 AmCham Events/ Awards Gala: Olga Voronova, AmCham Board Member and Country Manager, Procter & Gamble Kazakhstan reported on AmCham's many events throughout the year. *Monthly Sundowners, Seminars, Business Roundtables*, a high profile full-day conference in Astana devoted to *Challenges to Economic Diversification*, and above all, the annual black-tie *AmCham Awards Gala*, our most prestigious event of the year, were organized and delivered to the highest standard for CEOs, the business community at large, the diplomatic corps, and government officials.

The Gala presents 13 AmCham Awards for a diverse range of achievements by companies and individuals adjudicated by an arms-length Selection Committee. Categories include *CEO of the Year, Women's Leadership, Entrepreneurship, Healthcare, Community Service, Support for Kazakh Culture*, and many other achievements. The first award of the evening is always the *U.S. Ambassador's Award for Best Contribution to U.S.-Kazakhstan Relations* awarded to a prominent government recipient. Over the ten years of the Gala's existence more than one hundred awards have been presented to AmCham companies and corporate leaders for outstanding achievements.

2018 AmCham Publications: AmCham attaches special importance to its publications, the voice of AmCham in Kazakhstan and worldwide: *Investors' Voice (IV)*, the AmCham flagship publication continues its track record as 'Central Asia's leading business magazine', as it has been termed by the EBRD.

AmCham also regularly produces full-length *White Papers* for the Government, and in 2018, two Papers were produced: the 52-page *Improving Kazakhstan's Investment Climate: Barriers to Foreign Investment*, presented to the Prime Minister and Cabinet in March, and *Building a World-Class*

Healthcare System in Kazakhstan, presented to the Prime Minister and Health Minister in June. Both White Papers were produced in English and Russian.

AmCham also produces a 50-page *Annual Report* each year that is distributed at the *Annual General Meeting*, to the membership, diplomatic community, and is continually distributed year-round. In addition, a 150-page *AmCham Membership Directory*, a valuable resource guide to the membership is produced for CEO use and distributed year-round.

2018 Financial Report/ 2018 Board Election Results:

The Annual General Meeting concluded with the *2018 Financial Report* and *2019 Board Election Results* delivered by Ashley Clarke, KPMG Chief Operating Officer and AmCham Board Secretary. The Financial Report showed a balanced and healthy budget with judicious use of AmCham funds from membership fees, advertising revenue, and sponsorships.

The 2019 Board Election resulted in two re-elected Board Members:

- *Bela Ferenczi, AmCham Board Vice-President and General Electric CEO for Central Asia and Azerbaijan*
- *Paul Cohn, AmCham Board Treasurer and EY Central Asia and Caucasus Assurance Partner*

And three new Board Members:

- *John Baltz, Managing Director of the Chevron Eurasia Business Unit*
- *Tibor Kolejak, General Manager of Microsoft Kazakhstan*
- *Saule Zhakayeva, Deputy Chair and Corporate Banking Head, Citibank Kazakhstan.*



AmCham Board Members with Ambassador Brousseau,
New Members John Baltz (Chevron) and Saule Zhakayeva (CitiBank)

The AGM Sundowner that always follows the Annual General Meeting celebrates a successful year for AmCham, introduces the new Board Members, and marks the re-election of those members of the Board Executive Committee who stood for re-election. As always, an elegant and sumptuous buffet dinner with wine and an assortment of drinks was provided by the Rixos Almaty Hotel, the location of the AGM and the Sundowner.

Citi generously sponsored the Sundowner as it celebrated Citi's 25th anniversary in Kazakhstan. In 1994, Citi opened a representative office in Almaty, and in 1998 a full Citibank Kazakhstan subsidiary was established. Today, with offices in six cities, Citi is one of the country's largest banks by volume of payments and the only global financial brand with an operating license in Kazakhstan. Over the years Citi helped raise US\$30 billion in debt

financing for the government and others issuer and borrowers in Kazakhstan. Citi is proud to be recognized by the government as one of Kazakhstan's largest foreign investors. Last year the capital of Citibank Kazakhstan reached an equivalent of US\$400 million.

Citibank Kazakhstan is honored to be the bank of choice for almost all of Kazakhstan's major foreign investors and for most members of the American Chamber of Commerce in Kazakhstan. As in all 98 countries where Citi is present, in Kazakhstan Citi is keen to support the AmCham agenda and is pleased that AmCham has grown into one of the most influential business associations in the country.

Citibank CEO Andrey Kurilin, a former AmCham Board Member and member of the Board Executive Committee delivered a warm welcome to the evening's Sundowner guests and introduced the Board's new members.





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MEMBER NEWS



Kaspars Kukelis Appointed Chief Executive Officer of Kcell



Kcell, the leading provider of mobile telecommunications services in Kazakhstan, recently appointed Kaspars Kukelis as the company's new Chief Executive Officer.

Kaspars Kukelis has over twenty years' experience in the telecommunications industry, having held a number of senior level management positions at a variety of companies. Prior to Kcell, he served as Senior Retail Director at Kazakhtelecom and was a member of the company's Management Board. He also served as an Independent Director at Altel and as Kcell Marketing Director, after which he was promoted to Chief Commercial Officer.

Kaspars Kukelis graduated in Economics from the Kazakhstan State Academy of Management and holds an EMBA degree from Harvard Business School. In addition, he serves as Honorary Consul of Latvia.



VEON Appoints Evgeniy Nastradin Chief Executive Officer of Beeline Kazakhstan

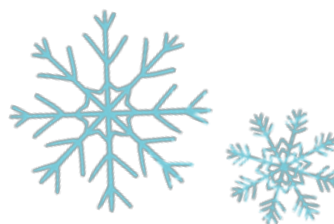
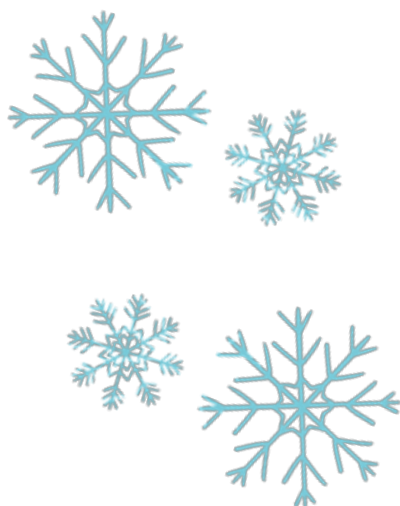


VEON, a leading global provider of connectivity and internet services, announces the appointment of Evgeniy Nastradin as CEO of Beeline Kazakhstan.

Evgeniy Nastradin first joined VEON in 2016 as Chief Commercial Officer of Beeline Kazakhstan during a period of solid revenue growth and the launch of new digital services. Prior to VEON, he was Deputy CEO of a leading consumer finance company in Russia.

Ursula Burns, VEON's Chairman and CEO, commented that "Evgeniy brings impressive experience across different sectors to his role as CEO of Beeline Kazakhstan. The Beeline brand has a large and growing customer base in Kazakhstan and we are seeing early, positive signs that its mobile financial services are gaining traction. I wish Evgeniy every success as we look to build on our strong position in Kazakhstan."

Before embarking on a career in business, Evgeniy earned his pilot's license from the Kremenchug Civil Aviation Flight School in 1995, and later continued his studies at the Kirovograd Civil Aviation Flight School, earning a degree in engineering. In 2014, he graduated from Odessa National Polytechnic University with a degree in business economics.





Erdinc Guzel Appointed General Manager of Coca-Cola Kazakhstan



Erdinc Guzel was recently appointed General Manager of Coca-Cola Kazakhstan after his successful assignment as General Manager of Coca-Cola in Azerbaijan, where he served for three years. In his new role, Erdinc Guzel is responsible for all company operations in Kazakhstan. He is a committed leader and business partner in Central Asia, bringing nearly a decade of Coca-Cola management experience to his new position.

Erdinc Guzel began his professional career in 1999 as Regional Sales Coordinator at Nestle, later holding executive positions such as Key Account Operations Manager and Sales Center Manager for Western Turkey. In 2009, he joined the Coca-Cola family, first serving as Commercial Manager for Azerbaijan, after which he moved to Coca-Cola Kyrgyzstan as Commercial Director in 2013 and was later appointed General Manager in 2014.

Erdinc Guzel graduated from Middle East Technical University in Ankara with a degree in Economics and Administration.



New KIS on the Block

Kazakhstan International School celebrates its 20th anniversary in 2019, and has much to celebrate.

In 1999 a new kindergarten opened in Almaty, with ten children and their teacher. Using the Montessori Method of education, the new kindergarten empowered children to explore and discover the world around them, emphasised play as part of a child's learning, and developed the children's character as well as their academic skills.

Over the years, the kindergarten became Kazakhstan International School (KIS). KIS grew and adopted the International Baccalaureate programme. By 2008, KIS was a fully fledged primary school accredited by the International Baccalaureate Organisation (IBO) to run the IB Primary Years Programme. The school moved to two sites – a kindergarten and a grade school - and steadily grew to over a hundred young children and students from Pre-Kindergarten to Grade 7.



In December 2018 KIS moved to its stunning new campus on a leafy hilltop above Al Farabi/ Remizovka. With students representing over 20 nationalities and teachers from twelve different countries, KIS provides an English-speaking environment in which diversity and international-mindedness is part of daily life. KIS student intake is evenly split between Kazakhstani students and those from expatriate families. KIS will soon offer the full IB programme, including the IB Diploma.

The IB ethos promotes lifelong learning and developing the key personal qualities children need as they mature into young adults. IB graduates are sought-after by leading universities worldwide because they are prepared not only academically, but also in terms of personal organisation and skills, global awareness, and willingness to be active and contribute to their community.

WELCOME ADDITIONS TO THE CHAMBER



Danone

CORPORATE A

Gilles Bourlot
General Manager

52 Abay Avenue
Almaty, Kazakhstan

Telephone: +7 771 501 1275

Email: gilles.bourlot@danone.com

Website: www.danone.kz

Danone is the world's number one fresh dairy producer. The Danone mission is to bring health through food to the maximum number of people. Danone has been active in Kazakhstan and Central Asia for more than 15 years. The Danone Berkut factory in Kazakhstan produces spoonable and drinkable yoghurts under the brands Danone, Activia, Rastishka, Smeshariki and Prostokvashino. Danone also produces a range of traditional dairy drinks such as Kefir, Ayran, and Tan under the brand Bio-Balance.

All these products are made from fresh milk supplied by farmers in Almaty Oblast with whom Danone has built a long-term partnership. Danone is very proud to have brought the same quality standards as those it applies worldwide to its local factory in Kazakhstan.



Capital Bank Kazakhstan

CORPORATE B

Yusuf Aslan
Chief Executive Officer

187B Nazarbayev Avenue
Almaty, Kazakhstan

Telephone: +7 727 331 6677

Email: info@capitalbank.kz

Website: www.capitalbank.kz

Capital Bank Kazakhstan is a fast-paced financial institution with more than 25 years of successful business, offering individual, corporate and SME banking services. Incorporated in 1992 as TAIB Kazakh Bank (Bahrain), the Bank was one of the first commercial banks operating in sovereign Kazakhstan. The Bank was renamed Capital Bank Kazakhstan in 2013.

In 2016, the Bank successfully launched the retail brand B1NK aimed at implementation of a number of large-scale retail business projects. Innovative high-tech processing and international standard scalable IT-platforms enable the Bank to offer its customers a variety of banking products on a very competitive basis, including unsecured consumer and car lending, as well as corporate financing instruments and mobile applications.

With due regard to the Bank's strengths and competitive advantages - high capitalization and liquidity, stress resistance, flexibility, mobility, high quality service and rapid decision-making - the Bank will continue to focus on developing into one of the top customer-focused and technological banks on the market.



CNP Processing

CORPORATE C

Chris Haney
Member of the Board

118 Shevchenko Street, Office 331
Almaty, Kazakhstan

Telephone: +7 (727) 244 04 77

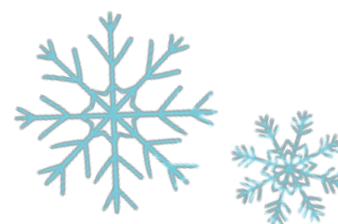
E-mail: aygerim.danyarova@processing.kz

Website: www.processing.kz

CNP Processing GmbH is the first non-bank e-commerce processor that offers bank card internet payment options to Kazakhstan merchants and banks. CNP Processing GmbH, under the service mark Processing.kz, has contracts with major Kazakh banks to provide payments and transfers to over 300 local merchants including Beeline, Altel Tele-2, Qazaq Air, Sulpak, e-gov, and Francuski Dom.

CNP Processing is the first non-bank processor operating in Kazakhstan to be fully certified by VISA and Mastercard. CNP Processing servers are located in Geneva, Switzerland with company staff located in Almaty.

In addition to standard Internet card payment services, CNP Processing provides customized ecommerce services to allow corporations to maximize payment processing efficiency with suppliers/customers, increase customer satisfaction and loyalty, and reduce procurement/sales costs.





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AMCHAM ADVOCACY UPDATE

JANUARY - FEBRUARY 2019

The first two sessions in 2019 of the *Council to Improve the Investment Environment* were held on 25 January and 21 February, devoted to two very different topics, one traditional and one quite new. The traditional topic in January was *Tax Reform – A Fresh Look at Kazakhstan's Tax Code*, a topic addressed each year at the Council, given the continuously changing nature of Kazakhstan's Tax Code. The February Council topic was *Cybersecurity and Cybercrime – A Challenge for the 21st Century*, in response to the ever-increasing global threats posed by a growing range of cyberattacks on governments, companies, and individuals.



January 2019 – Tax Reform – A Fresh Look at Kazakhstan's Tax Code

Kazakhstan's Tax Code underwent revision last year – supposedly to the benefit of investors, whom the Government promised in future would be given the 'benefit of a doubt' in tax disputes. In fact, according to tax experts, the revisions were fairly minor and did not alter the Government's assumption of criminality for tax evasion that continues to be retained in tax disputes.

With a new Finance Minister (*Alikhan Smailov*) replacing *Bakhyt Sultanov*, who had frequently supported AmCham, it was one of the purposes of the Council session to reaffirm the importance of the *Inter-Ministerial Tax Reform Working Group*, which meets monthly with the State Revenue Committee (SRC) under the Finance Ministry, and to win his support.

The Council speaker list was heavily weighted towards tax experts with three speakers from the Big Four audit firms plus Raimbek Batalov, a noted public advocate for small and medium businesses and the need for reduced government interference in these businesses. Excessive tax burdens and persistent tax audits are one of the reasons, in his estimation, that SMEs have a short life span in Kazakhstan. The 3 tax experts from the Big Four agreed on interlocking themes for their presentations to highlight the need for reform of long-standing tax issues that would ultimately serve to reduce litigation and lessen the burden on both investors and courts:

- *Explanation/ interpretation of items in the Tax Code to be provided by the SRC upon request (objective – centralized and binding explanations that could be relied upon by taxpayers in preparing their tax returns)*
- *Decriminalization of tax disputes – no assumption of deliberate fraud or tax evasion unless proven (often used as leverage to force additional tax payments)*
- *Reduction or elimination of re-audits after tax refunds are issued (no recalculation of refunds following their issuance and no penalties imposed on taxpayers for SRC 'errors' in calculating refunds)*

The 3 practices above are responsible for many lengthy legal disputes that could be eliminated altogether if the SRC could accept that most investors do not aim to misstate or evade taxes, and if the SRC would respond to queries during preparation of tax filings. The speakers did not oppose the principle that deliberate tax evasion or intention to defraud is a criminal offense but insisted that intent must first be proven before taxpayers are threatened with criminal prosecution.



In addition, the growing disparity between international tax standards and Kazakhstan's tax legislation and practices was highlighted in that it leads to additional misunderstandings between the SRC and taxpayers who wish to submit properly calculated tax returns but are unable to receive proper guidance.

The 4 Council Ambassadors (U.S., U.K., E.U. and Canada) each called for changes in tax administration supporting the inter-locking themes of the Big Four, and each emphasized the need to decriminalize tax disputes if there was no proof of intent to defraud the government. This has been an ongoing issue for many years that AmCham has raised repeatedly, but the government response has been limited to raising the tax threshold for criminal prosecutions without proof of criminality, a gesture that lacks impact given the size of most investor tax returns, in particular those of the oil industry.

Although the new Finance Minister was opposed to a significant change in any of the 3 issues, in follow-up discussions with Deputy Prime Minister Yerbolat Dossayev,

a former National Economy Minister now responsible for economic issues in the Prime Minister's Office, progress appears to be made on 2 of the 3 issues raised at the Council. Unfortunately, this does not extend to decriminalization, which the SRC appears entirely opposed to mitigating.



February 2019 – Cybersecurity and Cybercrime, A Challenge for the 21st Century

The February Council session was held on 21 February, which unexpectedly turned out to be the day on which the Prime Minister and entire Cabinet of Ministers submitted their resignations, ie were dismissed by President Nazarbayev. The formal announcement from the President was not made public until the evening, causing uncertainty throughout the day as it became clear that a Government upheaval was in progress, but without explanation.

Nonetheless, the afternoon Council session and the traditional morning meetings between speakers and Ministers were held on schedule, although the Prime Minister was replaced as Council Chairman in the afternoon by Deputy Chairman Timur Suleimenov, Minister of the National Economy, and a number of Ministers were replaced by Deputy Ministers.

The Council session was well-attended, given the nature of the topic and the presence of corporate executives specializing in cybersecurity who had travelled from Brussels, Warsaw, Moscow, and Istanbul for the Council. Foremost among these was Microsoft, which delivered the lead presentation and received numerous meeting requests from the Justice Ministry and other Ministries during their visit to Kazakhstan.

Cybersecurity is an outgrowth of AmCham's steady interest in and promotion of Intellectual Property Protection under the AmCham Inter-Ministerial Intellectual Property Working Group that has operated together with the Ministries of Justice and Healthcare for the past five years. The subject has acquired increasing importance globally in recent years due to high-profile cyberattacks on prominent corporations, banks, hospitals, and large governments.

Kazakhstan has also been hit by cyberattacks that have incapacitated corporations and oil companies, even though their cyber protective measures have been comprehensive. Given the wide-scale use of pirated technology across Kazakhstan, including by the Government (Microsoft estimates 75% of its software is pirated in Kazakhstan), vulnerabilities to cyberattacks are high. Critical infrastructure could be targeted with devastating results, but the Government does not appear to have addressed this issue seriously despite the recent emphasis on digitalization.

While most Council sessions aim to resolve investor problems, the February session was intended as a 'wake-up call' for the Government. Investors and companies are responsible for their own cybersecurity – for better or for worse, depending on their resources – but the Government is believed to be unprepared for serious cyberattacks.

Thus, AmCham composed a panel of 4 corporate speakers who could address the topic from different perspectives, but with one over-riding message for the Government. The speakers were from the oil industry, the financial industry, technology, and one of the Big Four with expertise in cybersecurity. They addressed the danger to the country's critical infrastructure, communications, and on a more personal level, identity theft. The four Council Ambassadors outlined their countries' approach to protecting government communications, data, and critical infrastructure.

The Government added to this Council session Ministers not normally part of the Council – notably from the Ministries of Communications and Defense and Aviation (the latter responsible for coordinating Government cybersecurity policy) - thus demonstrating their understanding of the extent of the security risk to the country in an age of frequently devastating cyberattacks.

Follow-Up with Prime Minister – Fair Competition Proposal from OECD

At the end of the October 2018 Council session devoted to *Creating a Level Playing Field: Competition vs Discrimination*, the Prime Minister requested that AmCham identify foreign experts who could assist in reforming the country's anti-monopoly legislation and creating fair competition practices.

AmCham approached OECD, which designed a new *Fair Competition Program* ('*Fighting Concentration and Anti-Competitive Practices, Improving Access to Markets in Kazakhstan*'). This proposal was presented to the Prime Minister at the end of the January 2019 Council Session. It is expected to present a formal response to the OECD during the AmCham Executive Director's OECD meetings in Paris in March.

AMCHAM WORKING GROUP UPDATE

JANUARY – FEBRUARY 2019

Almaty Working Groups

Almaty Technology and Innovations Working Group

January On January 22, the Almaty Technology and Innovation Working Group met in the AmCham Boardroom under new Group Chairman Tibor Kolejak, General Manager of Microsoft Kazakhstan. The Chairman began with a presentation on business technology and its role in reshaping traditional enterprises, after which the Group discussed how new cloud programs and software simplify routine businesses processes and avoid unnecessary bureaucracy. The floor was then turned over to Sanzhar Myrzagalym, Microsoft Cloud Solutions Architecture, who presented on current breakthroughs in artificial intelligence (AI) and machine learning, and demonstrated cognitive AI programs.



Almaty Corporate Social Responsibility Working Group

February On February 8, the Almaty Corporate Social Responsibility Working Group met under new Chairman Asad Shirinov, Country Manager for Coca-Cola Kazakhstan and Kyrgyzstan. Mr. Shirinov delivered a short introduction on the Group's purpose and goals, following which the floor was turned over to Alexandra Akkirman, Coca-Cola Public Affairs and Communication Manager, who gave a presentation on Coca-Cola's CSR strategy, highlighting progress in 2018 and plans for 2019. The Group reviewed its CSR strategies: community well-being, female empowerment, recycling, and nature protection. After the presentation, the Group discussed CSR projects in their respective companies.

Almaty Healthcare Reform Working Group

February On February 19, the Almaty Healthcare Reform Working Group met in the AmCham Boardroom, chaired by Ksenia Babushkina, EY Partner and Head of Advisory Practice. The session was devoted to outlining and discussing recent changes in Kazakhstan's Health Code. Andrei Yorsh, Baker & McKenzie Partner, delivered comments on the current legislation and answered questions. Members then shared their personal opinions on the Code and discussed its benefits and potential problems.

Astana Working Groups

Astana Trade and Customs Working Group

February On February 11, the Astana Trade and Customs Working Group met in the EY Astana office. After the introduction, the floor was turned over to EY Senior Manager Aizhan Sumembayeva and EY Senior Associate Dauren Rakhymgozhin, who delivered a joint presentation on transfer pricing and customs. The speakers focused on interrelations and contradictions and discussed different methods for transfer pricing.

Members discussed the advantages and disadvantages of each method. In the second part of the meeting, Sholpan Dossymkhanova, Deloitte Caspian Region Customs/Tax Manager, presented on product traceability systems, discussing WTO tariffs, virtual-warehouse modules, and E-Declarations, after which she answered questions.



Astana Human Resources Working Group

February On February 11, the Astana Human Resources Working Group met in the EY Astana office under EY Senior Manager and Group Chairman Damir Deminov., Almira Abraimova, EY Senior Manager, presented on recent changes in Kazakhstan's immigration legislation. The speaker outlined changes in work permits, visa rules, and entry regulations. Group members then shared their own issues with work visas and procedures for hiring foreign employees. The Group also discussed problems with the current legislation, including expansion of work permits in certain administrative units.



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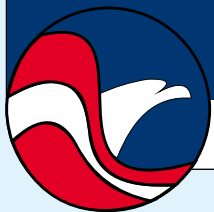
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AMERICAN CHAMBER OF COMMERCE IN KAZAKHSTAN

MEMBERSHIP APPLICATION

ABOUT AMCHAM

Registered in Kazakhstan as a non-profit organization in March of 1999 with 36 charter members, the **American Chamber of Commerce** in Kazakhstan currently represents over 200 member companies including US, multinational, and local businesses in 30 industry sectors. Their collective investment in Kazakhstan's economy is several billion USD. The AmCham in Kazakhstan is a member of the US AmCham of Commerce in Washington D.C. and has working relationships with many regional business associations.

BENEFITS OF MEMBERSHIP

- ✓ AmCham members participate in an organization existing solely to serve members
- ✓ AmCham actively advocates for reform of the business environment with Kazakhstan Government at senior levels
- ✓ AmCham Members may attend 19 Working Groups in 5 cities plus Inter-Ministerial Working Groups
- ✓ Monthly speaker luncheons with senior government and business leaders are reserved for AmCham members
- ✓ Seminars, conferences, and monthly social networking events are organized for AmCham members
- ✓ AmCham membership contact lists are available exclusively to AmCham members
- ✓ Economic, political, legal, social, and business development information is distributed to members
- ✓ Member companies provide exclusive discounts on products and services to other AmCham members
- ✓ Access to the Members' Only section on the AmCham Website
- ✓ Publishing opportunities are available in *Investors' Voice*, the *Annual Membership Directory*, and *Special Publications*

MEMBERSHIP APPLICATION

Company Name:

Industry Area:

CEO Name, Signature, Email:

Contact Individual:

Title(s):

Address:

Tel.: Fax: E-mail:

Please include us in the following Working Groups:

Almaty (7)

- | | |
|--|--|
| ☐ Foreign Investment | ☐ Healthcare Reform |
| ☐ Human Resources | ☐ Trade and Customs |
| ☐ Tax | |
| ☐ Technology and Innovation | |
| ☐ Corporate Social Responsibility | |

Atyrau (4)

- | |
|--|
| ☐ Tax |
| ☐ Human Resources |
| ☐ Trade and Customs |
| ☐ Corporate Social Responsibility |

Aktau (3)

- | |
|--|
| ☐ Human Resources |
| ☐ Tax |
| ☐ Trade and Customs |

Astana (4)

- | |
|---|
| ☐ Foreign Investment |
| ☐ Tax |
| ☐ Trade and Customs |
| ☐ Human Resources |

Shymkent (1)

- | |
|---|
| ☐ Foreign Investment |
|---|

WORKING GROUPS

Working Groups made up of representatives from our member companies provide comment, discussion and submission of positions and represent the united interests of the business community in Kazakhstan by identifying challenges faced by investors and proactively addressing them. Each group meets regularly, providing a forum for networking and the exchange of information. Groups are formed on an as-needed basis at the request of our membership.

GOVERNANCE

The AmCham is governed by a Board of Directors elected annually from and by the membership. Directors currently and in the past have included individuals from the following company members:

AES	HSBC
AIG Insurance	Hyatt Hotel
Baker & McKenzie	Intercontinental Almaty Hotel
BASF Central Asia	KIMEP
Bracewell & Giuliani	KPMG
BG Group	LeBoeuf, Lamb, Greene & MacRae
Capital Bank	Nestle
Chevron	PetroKazakhstan
Citibank	Philip Morris Kazakhstan
Conoco Phillips	Philips Kazakhstan
Coca-Cola	PricewaterhouseCoopers
Dechert	Procter & Gamble
Deloitte	Raytheon
DUCAT	Scot Holland CBRE
EBRD	Tengizchevroil
Ernst & Young	USAID
GE International	Visor Capital
Halliburton	White & Case
Honeywell	Procter and Gamble

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Resident Representative, Atyrau
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MEMBERSHIP CATEGORIES AND ANNUAL FEES

Corporate A	(Worldwide revenues in excess of 100 million USD)	\$5,000 USD
Corporate B	(Worldwide revenues between 2-100 million USD)	\$3,800 USD
Corporate C	(Worldwide revenues not exceeding 2 million USD)	\$2,700 USD
Non-Profit		\$1,500 USD
Individual**		\$500 USD

Corporate membership entitles a company to delegate 3 individuals as AmCham voting members. The number of persons from each company participating in working groups, forums, and business roundtables is usually not limited.

**Individual memberships are available only under special circumstances, for persons not associated with a company.

All applications for membership must be approved by the Board of Directors of the American Chamber of Commerce in Kazakhstan. For further information about membership benefits, the application process, or Investors' Voice magazine, please contact: info@amcham.kz



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At Pfizer, we apply science and our global resources to bring therapies to people that extend and significantly improve their lives. We strive to set the standard for quality, safety and value in the discovery, development and manufacture of health care products. Our global portfolio includes medicines and vaccines as well as many of the world's best-known consumer health care products. Every day, Pfizer colleagues work across developed and emerging markets to advance wellness, prevention, treatments and cures that challenge the most feared diseases of our time. Consistent with our responsibility as one of the world's premier innovative biopharmaceutical companies, we collaborate with health care providers, governments and local communities to support and expand access to reliable, affordable health care around the world. For more than 150 years, Pfizer has worked to make a difference for all who rely on us.

Pfizer H.C.P. Corporation (Kazakhstan)

Pfizer is the world's premier biopharmaceutical company, with operations in more than 150 countries. Pfizer has been present in Kazakhstan since 1995 is representative office was established in Almaty in 2001, and from year to year its focus and commitment to the local market has increased. Within 20 years, Pfizer Kazakhstan has become one of the strongest pharmaceutical companies on the local market, working with Government of Kazakhstan to find solutions through innovations and high quality in oncology, vaccination, rheumatology, hematology and other areas. Pfizer is also active in conducting clinical assessments of new medicines, and this also applies to Kazakhstan.

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