

# Doing Business Guide Kazakhstan 2006



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## KEY STATISTICS

## Republic of Kazakhstan

<b>Total Area:</b>	2,724,900 sq. km.
<b>Estimated Population:</b>	15.3 million (2006)
<b>Capital:</b>	Astana: 490,000
<b>Other Principal Cities:</b>	Almaty: 1.5 million Karaganda: 800,000
<b>Languages:</b>	Kazakh (official language) Russian (language of international communication)
<b>Neighboring states:</b>	Uzbekistan, Turkmenistan, Russia, China, Kyrgyzstan
<b>Currency:</b>	Kazakh Tenge (KZT)
<b>Exchange rate:</b>	KZT 121.48=USD1 (31 May 2006)

## EXECUTIVE SUMMARY

Modern-day Kazakhstan is a paradox. It hosts relatively sophisticated systems of internal communication, transportation, industry, agriculture, education, housing and health care, although most of the infrastructure suffers from funding restrictions. Kazakhstan is continuing to develop systems of business law, taxation, banking, and external links to the international business community and, most importantly, a market economy.

This paradox presents a unique challenge to business people entering Kazakhstan when attempting to assess real business risks and to make reality-based decisions rather than relying on perceptions. Abundant natural resource wealth and agricultural production make Kazakhstan's population one of the potentially richest countries per capita in the former Soviet Union. However, converting this potential into reality requires many critical factors to function in concert. Attracting and protecting investors is among the most critical of these factors.

As with many developing economies seeking external investment capital, Kazakhstan finds itself in a highly competitive situation. The wealth of its petroleum, mining, and agriculture sectors may be too great a temptation for many foreign investors to pass up. The question will be whether Kazakhstan's legal and business infrastructure will be able to keep pace with the demands inherent to investment development. Kazakhstan has successfully introduced concepts of property ownership, human rights, environmental protection and investment protection. In so doing, Kazakhstan has taken a giant step in meeting these development needs. New laws that appear to be consistent with the intent of the constitution are written and adopted with regularity. However, a number of operational regulations and legal practices are based on or derived from Soviet law.

In spite of some world-wide market fluctuations in the last few years, of late there seems to be a resurgence of interest in Kazakhstan among foreign investors. Coupled with recent political events in the region, many around the world seem to be focusing a little more closely on Central Asia as a whole.

Investors, whether multinational oil companies or small trading companies, continue to weigh the risks associated with Kazakhstan investments and are mindful of the impact that a fluctuating commodity price, like oil, can have on this emerging economy that depends heavily on its natural resources.

This business guide attempts to outline the various factors that should be considered by foreign enterprises deciding to invest in Kazakhstan. Rather than providing a detailed treatise on any one subject, the parameters of which are constantly in motion, this guide strives to cover a spectrum of issues that an investor would include in their "mission checklist" as they are entering Kazakhstan.

We hope you find the format of the guide enjoyable and the content informative. PricewaterhouseCoopers intends to update this guide regularly as time unveils new changes in legal, tax and business issues in Kazakhstan. If you are interested in obtaining these updates, contact your local PricewaterhouseCoopers office.

Good luck with your new business venture in Kazakhstan!

## HISTORY

### The People, The Land

Kazakhstan, a vast land of spreading steppe and rugged mountains, is the largest landlocked country in the world. The ancient inhabitants of Kazakhstan developed civilizations in the south over two millennia ago, leaving gold and ceramic relics for archaeologists. Probably considered the greatest relic and now a national symbol of Kazakhstan, the "Golden Man" is a sak warrior clad completely in gold clothing.

The Kazakh people of today emerged from the nomads that inherited the steppes, only to later surrender their nomadic life style under the Soviet system. They typically moved from the rivers in southern Kazakhstan to the north in summer in search of pastures, trading with those passing along the Silk Road. The temporary settlements of yurts, called "aul," were their only communities. Nonetheless, some settled more permanently in the south. When Islam spread to Central Asia around the 8th Century, it took hold in the southern settlements. The remaining Kazakhs adopted some philosophies from Islam and melded them with their own animistic beliefs. To this day, southern Kazakhstan tends to be more religious while, for some, Islam is merely a part of their heritage. Thus, the fundamentalism that spawned conflict in other parts of Central Asia has not affected Kazakhstan.

In the 13th century Genghis Khan's Mongolian army invaded the Kazakh Steppe. Genghis Khan left the area, now Kazakhstan, to be ruled by his three sons. The Western, Eastern and Central regions were given to the youngest, middle and eldest sons, respectively. This regional division became an identifying factor for the Kazakh tribes that lived in these Khanates and developed into the "zhus," or clan system, after the deterioration of the Mongol Empire.

With the continued threat of raiding tribes from the East, in the 18th century the Kazakhs turned to their neighbors in the north, the Russians, for military assistance. The Tsar was more than willing to help. The Tsar's Cossack forces had already founded Uralsk in western Kazakhstan and Ust-Kamenogorsk in eastern Kazakhstan. The fortress of Verniy was established in southeast Kazakhstan along the Tien-Shan Mountains in the 1854's, later to become the city known as Alma-Ata, and eventually Almaty.

The sparse steppe of southern Russia and northern Kazakhstan also became a dumping ground for the Tsar's unwanted. Russia exiled educated and cultured people to this region, including the Russian writer Dostoevsky. These individuals interacted with the Kazakh people, who eventually spawned the initial literacy among the nomads in the north and influenced such famous Kazakhs as the poet, Abai, and the geographer/scientist, Shokan Valikhanov. The Socialist Revolution and ensuing civil war that swept Russia were not without consequence for the Kazakhs. Bolsheviks established Kazakhstan as an autonomous region of Russia, which, in the late 1930's, became the Kazakh Soviet Socialist Republic. It was during this period that the Kazakh language adopted a Cyrillic alphabet, after having been penned earlier in Arabic script and, for a brief period, with Latin letters.

The onset of the Second World War brought more forced immigration to Kazakhstan. Stalin, faced with an invasion by the German Army, decided that certain ethnic groups could not be trusted near the fronts and had them moved to Kazakhstan. With the encroachment of the invading fascists, much of Russia's industry was moved beyond the Ural Mountains and even to Alma-Ata. The next wave of immigration from Russia was experienced in the 1950's with Krushchev's Virgin Lands Plan to cultivate the vast Kazakh steppe. By its independence in 1991, Kazakhstan developed a diverse cosmopolitan society, consisting of Kazakhs, Volga Germans, Koreans from the Far East, Poles, Crimean Tartars, Chechens, and Russians.

On 16 December 1991, Kazakhstan became the last republic to vote for secession from the Soviet Union and became an independent republic. With the Kazakhs now in total control of their independent republic, many of the non-Turkic ethnic groups emigrated. The trends, until recently, had been a negative population growth, averaging approximately 150,000 people a year since 1991, with the population of 14.8 million in 2003, compared with 16.7 million in 1991.

Even though politically independent from Moscow, most citizens of Kazakhstan continue to monitor Russian politics closely.

## The Politics

From 1964 to 1986, Dinmukhamed Kunayev held the position of General Secretary of the Communist Party of the Kazakh Soviet Socialist Republic. With Gorbachev's policy to reform the political nature and remove corruption, in 1986 Moscow appointed a Russian, Gennady Kolbin, as the new Party leader. Kolbin was the Communist Party leader in Kazakhstan for a very brief time before his successor, Nursultan Nazarbaev, rose to power.

In December 1991, President Nazarbaev, formerly the Communist Party's First Secretary for Kazakhstan, ran unopposed in the first presidential election. Nazarbaev began to embrace market-oriented reforms along what appeared to be Korean lines - autocratic leadership combined with a commitment to capitalist ideals.

In the spring of 1995, President Nazarbaev held a national referendum to extend his presidency for another five years, thereby foregoing the presidential election scheduled for 1996. The five-year term and two term limits for presidential rule in the constitution were changed by amendment in the fall of 1998. Elections held in January 1999 resulted in the re-election of Nursultan Nazarbaev for a term to the year 2006. In the latest presidential election held on 4 December 2005, Nursultan Nazarbayev won 91.1% of the vote and was re-elected for another six year term to the year 2012.

Today's government structure is based on the three-branch system, with an executive, legislative, and judicial branch. The President heads the executive branch. After several years of shuffling ministers and other high officials, the changes have since become less frequent.

Though Kazakhstan passed a new constitution as an independent state in January 1993, another constitution was passed by national referendum in the August of 1995. Both documents guarantee human rights and property ownership for all. In 2005, Kazakhstan ratified two new international treaties - the Pact on Civil and Politics Rights and the Pact on Economy, Social and Cultural Rights. According to the Constitution in force, Kazakh is the state language for Kazakhstan, with the Russian language being officially used along with the Kazakh language.

Despite the rotating cabinet members and other officials, reform continues. The last election was used in Kazakhstan as a reaffirmation of the President's power and popularity as well as an indicator of democratic progress. So far, Kazakhstan's opposition parties have failed to present a serious alternative to President Nazarbaev for a number of reasons.

The capital of Kazakhstan was moved from Almaty to Akmola, now renamed Astana, by presidential decree and was officially opened on 10 June 1998. Almaty remains the vital business and commercial center.



## ENVIRONMENT

The Soviet planning system, based on quantitative quotas for industry, has given rise to extensive environmental pollution in Kazakhstan. Soviet plans to develop the vast resources of Kazakhstan led to the adoption of ecologically harmful and wasteful processes for their extraction. As a result, Kazakhstan suffers from significant air and water pollution. Cities with high levels of air pollution include Almaty, Taraz, Zhyrnyyovsk, Temirtau, Ust-Kamenogorsk, and Shymkent.

Principal sources of pollution include non-ferrous metal plants that have not implemented suitable equipment for reducing waste emissions into the environment. Deforestation in eastern Kazakhstan has brought about soil erosion. Over-fishing in the Ural River and the Caspian Sea has significantly reduced sturgeon stocks. And, in western Kazakhstan, the chemical plants produce high levels of air pollution. Initially, there was a concern that the development of the Tengiz oil field would further pollute the area, principally due to sulphur dioxide gas emissions. To date, this has substantially not been the case.

Another victim of Soviet neglect is the Aral Sea. It may be considered one of the world's largest environmental disasters. Over the last 30 years, its surface area has fallen by more than 40% and its volume has dropped by more than 60%. This was primarily due to the Soviets draining contributory rivers of the Aral to irrigate land for cotton crops. Excessive use of fertilizers polluted local rivers and affected adjoining farmland.

The Aral problem is of global character and attracts the attention of world community. At a meeting in the capital of Kazakhstan-Astana in 2002 with Mr. Kofi Annan, the UN Secretary General, President Nazarbayev proposed to give to the International Fund on Salvation of the Aral (IFSA) the status of the UN Institution.

Experts think that it is impossible to restore the Aral Sea, but a hope still exists for the stabilization of the ecological situation there. The heads of the states-founders of the IFSA approved the Basic Directions of the Program of Actions on Improvement of Ecological, Social and Economic Conditions in the Aral Sea Basin for the period of 2003-2010 with a view to tackle the problem.

Nuclear testing (since 1949) also caused significant contamination around the testing site in Semipalatinsk and at the missile testing bases in Tyuratam and Saryshagan. Saryshagan and Baikonur were previously used in the Soviet space program. Nuclear testing ceased in Kazakhstan after 1989, largely due to the efforts mounted in the Nevada-Semipalatinsk antinuclear movement. Baikonur continues to be used by the Russians as their base for space launches and is currently being used as one of the space sites used in the launch of the multi-national space station, Alpha Project, as well as for missions to space station Mir prior to its recent return to earth, although Kazakh authorities have become notably cautious in allowing launches due to the caustic nature of the rocket fuel.

Now, Kazakhstan is boosting its ecological policy. In the field of the environment protection, new conceptual and program documents are being developed. The ecological legislation, economy, and society as a whole are becoming a priority direction of environment protection measures. This includes the introduction of strict ecological requirements in all legal acts, all sectors of the economy, and raising the public's general awareness.

Today, one of the most important issues is the improvement of nature conservation legislation with orientation to standards of the European Union, currently an important foreign trade and

investment partner. Kazakhstan, in simplifying the procedures of obtaining necessary permits while simultaneously toughening the ecological requirements, harmonized itself with the requirements adopted in the European countries.

The obligatory environment impact evaluation is currently introduced when any programme intended for the development of industry and agriculture and the allocation of industrial capacities, construction of urban areas, and other large-scale programmes, is proposed or undertaken.

From 2005, Kazakhstan introduced obligatory ecological insurance and ecological audits of environmentally harmful activities. The relevant laws are under development.

Kazakhstan has ratified 19 international conventions, including those of a climate change, destruction of ozone layer, desertification and preservation of a biodiversity, four transnational conventions of the European Commission and Aarhus Convention on ensuring the access of the population to information on ecology, decision-making and law maintenance in the field of environmental protection.

Aware of the danger to the environment, and the potentially disastrous effect that pollution could have on the world's caviar supply, Kazakhstan is actively promoting environmental protection programs, including actively encouraging the current and new oil producers to locate and properly seal Soviet-era wells. Despite its good intentions, and those of the other four countries bordering the Caspian Sea, the outlook for the Caspian environment remains tenuous, at best.

Currently, an Ecology Code is being considered by the Government. The draft includes provisions related to ownership rights for natural resources, implementation of international standards, evaluation of detrimental consequences, mechanisms for the stimulation of environmental protection and waste treatment.

## GOVERNMENT

### Republican government

The Government is responsible for the day-to-day functioning of ministries and agencies. The Government is chosen by, and is directly accountable to, the President and issues regulations in line with existing legislation. Unless specified by the Ministries as an issue to be resolved by the President or Parliament, the Government is also authorized to decide matters of economic management. The Government is accountable to the Parliament on questions of executing laws.

The Prime Minister is responsible for the direct management of the Government and can sign resolutions drafted by the Government or issue orders.

Aside from the Executive Branch, the government is comprised of the Legislative and Judicial branches. The bicameral Legislative Branch consists of the Senate (Upper House) and the Majilis (Lower House). The Senate contains 39 seats, seven of which are determined by Presidential appointment. Senate members serve six-year terms. The Majilis has 77 seats with five-year terms. The Supreme Court is elected by the Senate at the proposal of the President of the Republic of Kazakhstan.

Among the parties in Kazakhstan are: Otan (the party that supports President Nazarbaev), the Kazakhstan Civic Party and the Kazakhstan Agrarian Party (pro-president parties), the Communist Party of Kazakhstan, Ak Zhol (a splinter group of the former Democratic Choice of Kazakhstan), the Kazakhstan Patriots Party, the Kazakhstan Social Democrat Party-Auyl, and Asar (founded by the president's daughter, a pro-presidential association, to be constituted into a party).

### Local Government

Kazakhstan is divided into 14 administrative regions with separate administrative structures for a few selected cities such as Almaty. Local government budgets are subject to approval by local assemblies.

The head of the regional executive body, the Akim, is directly chosen by the President and serves as a representative of the President at a local level. The Akim's power terminates when a newly-elected President of the Republic is inaugurated, though the existing Akim will continue to perform his duties until the new President appoints a new Akim.

Regional governments are granted a limited amount of autonomy from Astana. An exception was made for the city of Almaty, which was granted extensive authority. However, economic decision-making is increasingly being de-centralized.

The capital of Kazakhstan was moved from Almaty to Astana from 10 December 1997. The inaugural celebrations for the new capital were held on 10 June 1998.

## The President

On 30 August 1995, a new constitution was approved in a referendum. The President was re-elected in 1999, his present term extending until 2006. On 4 December 2005, Nursultan Nazarbayev won 91.1% of the vote in the latest presidential election and was re-elected for another six year term to the year 2012.

The new constitution retains much of what was contained in the January 1993 constitution. Major differences include name changes, a detailed statement of the President's authority, the establishment of an Upper and Lower House of Parliament, and a provision that restricts the Parliament's ability to introduce legislation.

The Presidency is the highest executive authority in Kazakhstan. The President is elected for seven-year terms. Candidates for President must be not younger than forty and must have lived in Kazakhstan for not less than fifteen years as well as having a perfect command of the Kazakh language. The President not only represents Kazakhstan internationally but also chairs the Government and nominates the Prime Minister. The President nominates the Deputy Prime Ministers, and Ministers for the Ministries of Foreign Affairs, Defense, Finance, and International Affairs, etc. All nominees are subject to approval by the Parliament.

Additionally, the President is responsible for signing laws for the Republic and can return a law to Parliament for its re-consideration for up to one month. Should the Parliament vote (by a two-thirds majority) to accept the law in its original form, the President is obliged to sign it. If no objection is raised within the original one-month period, it is assumed that a law has been passed. The President is also empowered to form and abolish Ministries, state committees, and other government agencies. He can conduct negotiations, sign international agreements, grant citizenship, and appoint or replace diplomatic representatives.

## The Parliament

The Parliament is the supreme legislative body of Kazakhstan. Parliament consists of two Chambers acting on a permanent basis: the Senate and the Majilis. Senate deputies' terms are six years; the Majilis deputies serve five-year terms. As in Russia, the Parliament's role is to approve the prime minister and other key government positions nominated by the President. The Parliament is responsible for approving the Constitution and passing constitutional amendments, adopting laws and other legislation, exercising control over the implementation of legislation, and giving official interpretations of laws and presidential decrees. The Parliament also ratifies international treaties.

The last parliamentary elections were held on 19 September 2004. Otan, a party, led by Nursultan Nazarbayev, took almost all of the seats in the Majilis. Other parties that took seats in Majilis are as follows: Ak-zhol, Asar, and Aist (a coalition of the Civil and Country parties).

## Judicial Administration

Within the Judicial Administration, the Senate elects the Chairperson of the Supreme Court, the Chairpersons of the Justice Collegium, and judges of the Supreme Court of the Republic at the proposal of the President. The regional courts consider civil cases where one of the parties is an international or foreign organization.

## ECONOMY

Kazakhstan, the second largest of the former Soviet republics in land mass, possesses enormous untapped fossil fuel reserves as well as plentiful supplies of other minerals and metals. It also has considerable agricultural potential with its vast steppe accommodating both livestock and grain production. Kazakhstan's industrial sector relies on the extraction and processing of these natural resources and also on a relatively large machine building sector specializing in construction equipment, tractors, agricultural machinery, and some defense items. The dissolution of the USSR and the collapse of demand for Kazakhstan's traditional heavy industry products resulted in a sharp contraction of the economy since 1991, with the steepest annual decline occurring in 1994. In 1995-1997 the pace of the government program of economic reform and privatization quickened, resulting in a substantial shift of assets to the private sector.

The December 1996 signing of the Caspian Pipeline Consortium agreement to build a new pipeline from western Kazakhstan's Tengiz oil field to the Black Sea increased prospects for substantially larger oil exports for several years.

Kazakhstan's impressive economic growth continued in 2005 with GDP annual gross of 9.4%. Principal sectors within the economy are agriculture, non-ferrous metals, chemicals (including petrochemicals), fuel and energy resources. Industry now accounts for 31.5 % of the GDP, transport – 8.7%, trade – 14.2%, construction – 3.6%, agriculture – 1.9%, according to figures for 2005. Kazakhstan's chemical industry is a major producer of calcium carbide, sulphuric acid, phosphorous and chromium compounds. In recent years, production of mineral fertilizers has increased significantly. Kazakhstan is also home to the Aktau Plastics Factory, one of the largest producers of polyethylene in the CIS. Additionally, Kazakhstan also has large coal deposits in Karaganda, Ekibastuz, Maikubinsk, and Kushmurunsk.

Agriculture is shifting away from the Soviet-era focus on large harvests, and instead attempting to maximise revenue per hectare, particularly through exports. Improved harvest quality in recent years has led to higher exports.

Overall, around three-quarters of Kazakhstan's exports are intermediate goods and raw materials, while finished goods constitute a small part. About half of the finished goods consumed within Kazakhstan are imported. Kazakhstan's exports principally consist of: 60.2% hydrocarbons; 20% metals, of which more than one-quarter are copper and copper products; and the remaining 19.8% divided among grain, machinery, consumer goods and others. Most of the exports from Kazakhstan are to Russia, the Commonwealth of Independent States, the European Union, and China.

The largest importers tend to be Russia and the Commonwealth of Independent States, Germany, the United States and the European Union, with machinery and equipment representing a significant portion of the imports.

Kazakhstan has approximately 14,500 kilometres of railways that serve as a major means of transporting freight. Compared to some of the other former Soviet Republics, Kazakhstan has reasonably good road and air links to major cities in the CIS. Kazakhstan has a fairly well developed infrastructure with enjoyable cultural facilities and a relatively well-educated population.

Kazakhstan also has significant reserves of iron ore and non-ferrous metals including lead, magnesium, titanium, zinc, molybdenum, silver, copper, gold, tin, industrial diamonds, chrome, uranium, tungsten, bauxite, manganese, vanadium, beryllium, nickel, rhenium, and gallium.

With its natural resources, like oil, gas and metals, Kazakhstan is particularly attractive for foreign investments, attracting over USD 34 billion between 1993 and 2004. Most of the major oil companies are represented here. In particular, the Caspian Sea region hosts a number of activities centered on the oil and gas industry. Other foreign investment has been made in the cigarette industry, the energy and telecom sectors, as well as private lending to the government.

In comparison with many of the other former republics, Kazakhstan's economic structure is believed to be relatively well placed for the process of structural adjustment upon which it has embarked. Its rich mineral base and related industries, as well as the wide variety of agricultural goods produced, promise the development of a well-diversified economy.

Because of its strong macroeconomic performance and financial health, in 2000 Kazakhstan became the first former Soviet republic to repay all of its debt to the International Monetary Fund (IMF), 7 years ahead of schedule. In March 2002, the U.S. Department of Commerce granted Kazakhstan "market economy" status under U.S. trade law.

In September 2002, Kazakhstan became the first country in the former Soviet Union to receive an investment-grade credit rating from a major international credit rating agency.

**BUSINESS****Entity Selection**

Currently, Kazakhstan law allows for general partnerships, limited partnerships, limited liability partnerships, additional liability partnerships and joint-stock companies. Joint ventures, as well as other legal organizational forms, are defined as forms of a partnership. The law provides an outline illustrating the scope of activities permitted for entities, as well as procedures for registration, dispute settlement, and liquidation. In addition, accounting and reporting requirements are described.

A law "Concerning Joint-Stock Companies" came into force on 16 May 2003 that allows for two kinds of joint stock companies, depending on the authorized capital and number of shareholders. If an entity has more than 500 shareholders and an authorized capital of approximately USD 7.1 million (depending on current exchange rates), it is allowed to form or re-register as a Publicly-Held Joint-Stock Company. Otherwise, with a minimum of approximately USD 360,000 an entity can register as a Joint-Stock Company. The condition regarding the size of the authorized capital cannot be accepted if the company operates as an Investment Privatized Fund.

An entity previously registered as either an Open or Closed Joint-Stock Company had until 16 May 2005 to re-register, following the above criteria, in one of the new forms permitted. If not re-registered by then, the company has one year to either re-register or liquidate.

Affiliates of foreign companies operating in Kazakhstan can choose to register as a representative office or a branch. The choice of a corporate form is important because of the financial and tax implications of each. For example, representative offices cannot conduct commercial activities. The most common corporate structure of foreign companies with a presence in Kazakhstan seems to be a branch, followed by a representative office, limited liability partnership, and joint stock company.

Registering for activities is done by submitting a standard application, with attachments, to the Ministry of Justice or a judicial body situated where activities are (or will be) performed. In 2005, the registration rules were simplified. Documents to be submitted with the application include: a copy of the Charter or the Articles of Incorporation of the parent company; the Corporate Statement of the Branch or Representative Office; the Certificate of Incorporation for the parent company; and, a design for the seal of the branch or representative office. Many registrations can be completed within 10 days from the date that the required documents are submitted to the Ministry of Justice or its territorial bodies.

When registering a partnership, a single partner is usually sufficient. Founding documents should contain information on the type of partnership, its purpose and period of activity, its participants (founders), the company name and location, the charter fund, and the procedure for distributing profits and losses. The state registration of entities is completed by the Ministry of Justice, or by its territorial bodies. Registration should be completed within 10 days of submitting the required documents to the Ministry of Justice or to its territorial bodies.

In a number of cases, where the state registration is carried on by the tax authorities (e.g., foreign legal entities in Kazakhstan without forming a permanent base), the registration must be completed within 10 working days of beginning activities in Kazakhstan, although in some cases for non-resident entities the time limit is 30 days from beginning activities in Kazakhstan.

## Investment

On 5 May 2005, the Law "Concerning Investments in the Republic of Kazakhstan" was amended. The law replaced both the Law On Foreign Investments and the State Support Law previously governing investment activity in Kazakhstan and is viewed by the foreign business community as worsening conditions for new investors.

Based on the Law's provisions, preferences awarded to the investors on the basis of contracts signed with the state authority before adoption of this Law, should be effective until expiration of such contracts. This seems to provide a certain degree of confidence to the current investors in respect of their activities predating this law.

The Law is of a general nature and does not provide detailed regulations in respect of issues governed. That means that its practical application could be problematic, as it also requires consideration and application of other laws. Therefore, new investors will need to negotiate carefully and ensure that all their rights and obligations are clearly addressed and precisely defined in their investment contracts to mitigate the risk of misinterpretations in the future.

One should also remember that the practical application of general statements will be difficult and inefficient without support in other laws or an investment contract.

Below, we discuss in bullet points the most important issues addressed in the new Law.

- Definition of investments is limited to: investments into charter capital of legal entities; fixed assets used in entrepreneurial activities; and, property (except goods for personal use) and objects of financial lease on the basis of a leasing agreement.
- The Law provides investment incentives, which are restricted to investors who are Kazakhstan legal entities.
- Tax related investment preferences are not granted to investors for activities carried out under subsurface user contracts and to other taxpayers subject to special tax regimes.
- There is only partial stability provided under the Law.
- In case of termination of an investment contract, investors are liable for the payment of taxes and customs duties, which have not been paid due to the investment preferences.
- Investors' activities are subject to "supervision and control" of the state authorities.
- Investors should be reimbursed for any losses resulting from nationalization of assets (if any), whereas, in case of a requisition, only the market value of assets will be compensated.
- The oil and gas sector seems to be less attractive for investors due to: restrictions on tax related incentives in relation to subsurface user contract activities; limited stability of contract provisions; restrictions on incentives when the investor is not a Kazakhstan legal entity.

A model Contract for the execution of investments with the investment preferences was approved by Government Decree No. 436, dated 13 May 2003, establishing objects of



investment activity including investments in fixed assets. The tax preferences on corporate income tax, property tax, and land tax are granted to the investor. Further, the model contract stipulates the tax preference validity period. The Kazakhstan tax legislation allows those foreign investors investing in fixed assets for the purpose of creating new or upgrading effective production sites to take additional deductions from aggregate annual income.

## Licensing

Foreign investors are generally permitted to operate in any sphere of activity that is not otherwise prohibited by current legislation. However, activity in a number of sectors requires licenses from the authorized government offices. A license can be obtained by submitting an application and documents required by the governing office. Licenses can have limited or unlimited validity. Additionally, a license can be valid only in a specific region within Kazakhstan or for the entire territory of Kazakhstan. In certain circumstances, licenses can be required for activities conducted outside of Kazakhstan.

Certain activities require annual re-certification.

Foreign investors are generally not permitted to produce goods of a military nature, medicines, toxic substances, bank notes and coins, or to treat individuals with certain dangerous diseases (including dermatological, venereal, and psychological illnesses).

Before embarking on any activity, it is prudent to determine whether the activity requires licensing and whether the regulations of the governing office restrict the type of entity that can hold the license. For example, some licenses can only be issued to a resident, which excludes branches of foreign companies, but not to subsidiaries or affiliates. Licenses for certain activities can be issued to branches of foreign legal entities but they will often find them to be limited in their duration and/or scope.

A new licensing law is currently being considered by the Majilis. The law is generally aimed at simplifying licensing procedures.

In 2005, the Law on Technical Regulations replaced the laws on standardisation and certification.

## Real Estate

Almaty office space is usually less expensive than in Moscow or other European locations. In Almaty, however, prices are starting to catch-up despite the government's move to Astana. This is especially true in the new buildings that are closer to Western standards. Since a lot property is still state-owned, it is important to find out who has the right to rent property and on what terms.

A number of real-estate agencies in Kazakhstan can offer assistance in finding office space, as well as provide a number of other services for a reasonable fee (usually equal to one-tenth to one month's rent).

The regulations regarding foreign ownership of land and buildings continue to change. Additionally different authorities take varying and often contradicting views on the ownership of

land and/or buildings by foreign individuals and companies. We recommend checking with legal counsel for the latest interpretations.

Renting an apartment costs anywhere from USD 500 a month for a reasonable two-room apartment in the suburbs to as much as one is willing to pay for a five to six-room flat fully furnished (with local or foreign furniture) in the city's centre. When compared with salaries and other types of income, rental income is substantial for Kazakhstan citizens and provides them with a supplement. Again, it is important to confirm that the person renting the property has its legal ownership and, therefore, the right to lease the apartment. In addition, proper identification and a simple lease agreement in Russian and English should be obtained. Leases, at a very minimum, should state the terms of renting the property and should form the basis for a working relationship and understanding with a landlord. In some arrangements, the landlord agrees to cover utilities charges (except international phone charges) and to carry out basic repairs.

Activities associated with land usage and ownership are regulated by the Land Code of 2003.

## Employment

Currently, employment relationships in Kazakhstan are largely regulated by the Labor Law dated 10 December 1999. However, the Government is expected to issue a new Labor Code in 2007. According to the Labor Law, employment contracts define the terms of employment. Standard working hours are 40 hours a week, with special provisions for shift work.

Representative offices and branch offices with 100% foreign ownership are permitted to pay local employees in hard currency, which are generally made through bank transfers to employee accounts. The amount of work remuneration is established by the employer independently and it may not be lower than the minimum amount of work remuneration as established by Kazakhstan's legislation. For 2005 the minimum monthly wage is estimated at equivalent to USD 52 for January-June 2005 and USD 70 for July-December 2005. Nevertheless, wages tend to start at the Tenge equivalent of USD 300-400 a month. Employees, however, are quickly learning to appreciate a fair salary and salaries have been rising rapidly. Qualified specialists with good English skills often receive salaries that are comparable to western standards.

Many Kazakhstan enterprises contract employees based on net salaries. The appropriate individual income taxes are transferred to the Government Budget and the pension contributions to the Accumulative Pension Fund under a withholding tax mechanism. For more details, please see the section on taxation in Kazakhstan.

## Foreign Manpower

Currently, work permits must be obtained for all foreign employees in companies, branches and representative offices, except for the head or director of a branch or representative office, particularly within 60 days of beginning a Kazakh activity. Work permits can be difficult to obtain, sometimes taking as long as four-six months.

Work permits are obtained by submitting the required documents to the regional representatives of the Ministry of Labor and Social Protection and, including copies of employment contracts, educational and specialist certification, and an HIV certificate for each employee. The decision to

grant a work permit will depend on the ability to justify the need for the specific specialist in the Kazakh labor market.

When a work permit is granted, the employer deposits a guarantee/security payment in a bank account in an amount equal to the cost of a return ticket to the country of the employee's residence. The money will be returned to the employer when the employee leaves Kazakhstan.

Under the latest regulations, work permits are valid for a period up to one year. It is also worth noting that, under the current regulations, while visas are generally provided for the entire country of Kazakhstan, however work permits are now being issued for the specific region (Oblast) where they will be used (but the visa is valid for the entire country of Kazakhstan). There have been instances where the transfer of an employee from one region to another has created work permit issues requiring special attention.

Please be aware that the Work Permit Rules continue to change and are subject to a wide variety of local authority interpretation.

The Government has twice increased the 2006 quota for employing foreign labor in Kazakhstan: from 0.45% to 0.55% and from 0.55% to 0.70% of the Republic's economically active population. Currently, approximately 55,200 work permits are available for foreigners.

## Auditing and Accounting

Under Kazakhstan legislation, enterprises with foreign participation must undergo an annual audit. An audit company of choice can perform this audit.

The Law "Concerning Accounting and Financial Reporting" issued in December of 1995 defines the system of accounting in the Republic of Kazakhstan and establishes the fundamental principles and general rules for accounting. These principles and rules must be complied with when financial statements are prepared and used. The accounting method for financial purposes is accrual method

In September 2002, Kazakhstan adopted a new Chart of Accounts that was amended in October 2003. The Chart of Accounts is a basic classification system for income and expenses, through which the balance of an enterprise's profit or loss can be determined. The Kazakhstan Accounting Commission adopted new accounting standards, which are generally based on international standards. These new standards were in effect since 1 January 1997. Further, in May 2002 the Government amended the Accounting Law to adopt gradually the use of International Accounting Standards for Kazakhstan accounting purposes. According to the Law starting January 2003 banks and other financial institutions follow International Financial Reporting Standards. For Joint Stock Companies, the required move to IFRS is effective from 1 January 2005, and for other organizations, from 1 January 2006.

## Currency

Kazakhstan first issued its national currency, the Tenge, in November 1993. Then, on 5 April 1999, the National Bank of Kazakhstan ceased intervention in the currency's support and allowed the Tenge to freely float on the Almaty Financial Instruments Exchange (AFINEX).

A market exchange rate is fixed daily at the Kazakhstan Security Exchange (KASE). The market exchange rate is an average weighted exchange rate of Tenge to a foreign currency formed at a substantive session of the Kazakhstan stock exchange and determined in a procedure established by the Kazakhstan Ministry of Finance and the Kazakhstan National Bank.

According to Kazakhstan legislation, transactions between Kazakhstan legal entities should be in Tenge. Alternatively, transactions between a Kazakhstan legal entity and a foreign legal entity can be denominated in any currency.

Currency regulations dating back to 1996 state that retail trade in "cash" foreign currency will be prohibited regardless of an entity's status as a resident or non-resident. The currency regulations also state that all foreign currency transactions must be processed through an authorized bank, licensed non-banking financial institutions, or their exchange offices.

Currency regulations prohibit companies from using funds for non-registered business purposes. At this time, hard currency withdrawals can be made from a personal account with less documentation than from a corporate account. However, use of these funds for business purposes would constitute a violation of the regulations.

In 2005, a new currency law was adopted. The law was aimed at liberalizing the currency regime. However, it also introduced certain additional control and reporting requirements (e.g., branches are now subject to special currency monitoring).

## TRAVEL HINTS

## Visas

Kazakhstan requires a Kazakhstan visa for travel to the Republic. Also the Kazakhstan transit visa is mandatory, with the exception of Russian visa holders, if you are in transit (i.e., when you are traveling to another country through Kazakhstan). A transit can last no longer than three days. A visa usually costs between USD 35-400, depending on its status and term. A visa typically takes about two weeks to obtain. For more details on visas, contact the nearest Kazakhstan embassy.

Visas are sometimes difficult to obtain at airports on arrival in Kazakhstan, with the exception of diplomatic visas. Therefore, when checking in for a flight to Kazakhstan, the airline will check all documents, including visas, and might not allow a person on the airline if the documents are not in order.

Since there are few Kazakhstan embassies in the world, procuring a visa will require some organization and forethought. If there is no Kazakhstan embassy in your country, you may try to apply for a Kazakhstan visa in the nearest country with a Kazakhstan embassy or consulate.

In some countries, it may be possible to request that a Kazakhstan visa be arranged by a Russian embassy if a Kazakhstan embassy does not have a presence. It is worthwhile to confirm this with the Russian embassy first and to inquire about any additional documents that will be required.

When obtaining a visa through a Kazakh embassy or consulate, an invitation from a host organization in Kazakhstan, three passport photos and the completed application form (which should be available from the embassy) are usually required. The validity of passport should not expire earlier than three months after expiration of the requested visa. Upon receipt of the visa, confirm that the dates in the visa are correct and cover the period of stay. Should travel to other countries be included in the itinerary during the visit to Kazakhstan, ensure that the Kazakhstan visa is not limited to a single entry.

One-month, single-entry visas obtainable upon arrival to Kazakhstan are available to citizens of certain countries. Please check with the nearest Kazakhstan Embassy or Consulate to verify qualification for these simplified procedures.

**Belgium**

30 Avenue Van Bever,  
1180 Brussels, Belgium  
Tel: 32 (02) 374-9562  
Fax: 32 (02) 374-5091

**Canada**

347 Bay Street, Suite 600  
Toronto, Ontario M5H 2R7  
Tel: 1 (416) 593-4043  
Fax: 1 (416) 593-4037  
(Consulate)

France	Germany
59, rue Pierre Charron, Paris, 75008, France Tel: 33 (1) 4561-5200 33 (1) 4561-5206 Fax: 33 (1) 4561-5201	Nordenstrasse 14-17, Berlin, Germany 13156 Tel: 49 (30) 470-07-111 49 (30) 470-07-160 Fax: 49 (30) 470-07-125
United Kingdom	United States
33 Thurloe Square London SW7 2SD United Kingdom Tel: 44 (207) 581-4646 44 (207) 590-3480 Fax: 44 (207) 584-8481	1401 16th Street, N.W. Washington DC. 20036 Tel: 1 (202) 232-5488 1 (202) 550-9617 Fax: 1 (202) 232-5845

## Travel

Four of the well-known European airlines fly to Almaty and, together, give the traveler the opportunity to fly to and from Kazakhstan on every day of the week. Almost all flights arrive in Almaty between 00.00 a.m. and 04.00 a.m., under the current schedules:

Airlines	Flights to Almaty
British Airlines, London (Heathrow)	Monday, Wednesday, Saturday
KLM, Amsterdam	Monday, Tuesday, Thursday, Friday, Saturday
Lufthansa, Frankfurt	Six days a week: direct flights – Wednesday, Saturday; via Astana – Monday, Tuesday, Thursday and Friday.
Turkish Airlines, Istanbul	Seven days a week

To travel to Astana, most travelers fly into Almaty and then take Air-Astana to Astana. There are several flights in the morning and evening to and from Astana all days except Saturday and Sunday. There are now, however, a few flights into Astana from Moscow (Monday, Wednesday, Friday), Hanover (Thursday, Sunday), and Frankfurt (Wednesday, Friday, Sunday).

The national air carrier, Air-Astana, also operate most of the internal flights between cities in Kazakhstan. It currently also offers flights to some international destinations such as Budapest, Hanover, Beijing and Urumqi (China), Dubai, Istanbul, Bangkok, London, Seoul, Frankfurt, Amsterdam and Moscow. Trains frequently provide an airline alternative for journeys in Kazakhstan and to certain neighboring countries.

## Customs

Currently, customs declarations are required if items to be declared exceed USD 3,000, and/or more than USD 3,000 in cash. The customs declaration describes the currency and amount of money, valuables, and other items being imported. If a customs declaration is submitted, both forms would be stamped and one will be returned. The one that is returned must be submitted upon departure from Kazakhstan together with a departure declaration. The departure declaration again requests information concerning money and valuables being exported from the country. Typically, the authorities seek to confirm that valuables were not sold and that more money is not being taken out of the country than was brought in. Individuals are not permitted to take more than USD 10,000 cash out of the country. It is worth mentioning that Tenge may not be exported.

## Registration

Within five days of arrival in Kazakhstan, an individual is required to register with the Migration Police (former Office of Visa and Registration-OVIR). As proof of registration, the passport will be stamped with dates corresponding to the visa. If an individual does not obtain the required Migration Police stamp, a penalty fee may be assessed if stopped by the police or upon passport inspection at the airport during departure.

According to Kazakhstan legislation, foreigners must carry their passport with the visa and the OVIR stamp or, recently, a copy of all three (provided it is notarized by the foreigner's embassy) at all times. The police can stop anyone at any time and ask to see their documents. Failure to produce the requested document can result in detainment until the original passport is produced, complete with a visa, an OVIR stamp and, often, a penalty.

## Accommodations

In Almaty, travelers have several options for hotel accommodations, including the Hyatt Regency Almaty and the Regent Ankara – international five-star hotels; the Hotel Astana and Hotel Ambassador – international three-star hotels; Hotel Dostyk (former communist party hotel) and the Otrar Hotel (former Inturist hotel) – both well-known national hotels.

When traveling to Astana, one has fewer options, but business people who frequent Astana recommend the Intercontinental Hotel – international five-star hotel; Comfort Hotel, and Akku Hotel. In Atyrau - Hotel Atyrau, Shagala, The River Palace, Riverside Inn – are international hotels. In Aktau – Renaissance (Marriott hotels).

The hotels listed above accept all major credit cards. For more information on hotels and restaurants, please contact: PricewaterhouseCoopers in Almaty and ask for a copy of our PricewaterhouseCoopers Telephone Directory.

**Almaty****Hyatt Regency Almaty**

Rates: USD 260-1,725 (exclude 15% VAT)  
 Breakfast is not included  
 Tel: 7-3272-501-234  
 Fax: 7-3272-508-888

**The Regent Almaty-Ankara Hotel**

Rates: 295-3,740 USD (exclude 15% VAT)  
 Breakfast is not included  
 Tel: 7-3272-503-710  
 Fax: 7-3272-582-100

**Hotel Ambassador**

Rates: USD 150-265 (include 15% VAT)  
 Breakfast is included  
 Tel: 7 (3272) 508-989  
 Fax: 7 (3272) 698-441

**Astana Hotel**

Rates: USD 174-225 (include 15% VAT)  
 All major credit cards are accepted  
 Breakfast is included  
 Tel: 7 (3272) 50-70-50  
 Fax: 7 (3272) 50-10-60

**Hotel Dostyk**

Rates: USD 146-352 (include 15% VAT)  
 Breakfast is included  
 Tel: 7 (3272) 582-270  
 Fax: 7 (3272) 636-804

**Hotel Otrar**

Rates: USD 108-622 (include 15% VAT).  
 Breakfast is included  
 Tel: 7 (3272) 506-806  
 Fax: 7 (3272) 506-809

**Astana****Intercontinental Hotel**

Rates start at USD 299 (exclude 15% VAT)  
 Breakfast is included  
 Tel: 7(3172) 39-10-00  
 Fax: 7(3172) 39-10-10

**Comfort Hotel**

Rates start at USD 144 (include 15% VAT)  
 Breakfast is included  
 Tel: 7(3172) 221-021  
 Fax: 7(3172) 221-030

**Akku Hotel**

Rates: USD 115-225 (include 15% VAT)  
 Breakfast is included  
 Tel: 7(3172) 152-700, 152-950  
 Fax: 7(3272) 324-199



**Atyrau****Hotel Atyrau**

Rates: USD 175-620 (include 15% VAT)

Breakfast is included

Tel: 7(3122) 921-100, 921-110

Fax: 7(3122) 271-827

**Shagala**

Rates start at USD 160 (exclude 15% VAT)

Breakfast is included

Tel: 7(3122) 354-033, 328-490

Fax: 7(3122) 354-034

**The River Palace**

Rates start at USD 165 (exclude 15% VAT)

Breakfast is included

Tel: 7(3122) 355-241, 355-239

Fax: 7(3122) 355-236

**Riverside Inn**

Rates start at USD 85 (exclude 15% VAT)

Breakfast and laundry are included

Tel: 7(3122) 450-498

**Aktau****Renaissance (Marriott)**

Rates start at USD 225 (exclude 15% VAT). Breakfast included.

Tel: 7(3292) 300-600

Fax: 7(3293) 300-601

## BUSINESS TIPS

### Social Obligations

The foreign investor often becomes involved in local life and community activities by funding social projects or improving amenities. Public relations is very much a part of doing business in Kazakhstan. Recognizing and participating in local holidays, providing new equipment for local hospitals, new playgrounds for schools, providing educational materials, or sponsoring local youth teams are just some of the ways that foreign investors have assisted and contributed.

### Drivers

Drivers are a necessity for foreign business people in Almaty as business hours in Kazakhstan can be long and sometimes irregular. Drivers are most easily and reliably hired through the inviting organization. Current rates are about USD 10-12 per hour or USD 35 a day on a temporary basis. Very few drivers speak English or any other western European languages, however, more and more do understand directions and one should be able to communicate without a translator.

It is possible to hire a car from Europcar\*. Payment can be made by major credit cards like American Express, Visa, Diners Club, MasterCard/Eurocard. Both the Hyatt Regency Almaty and the Regent Hotel have hotel cars available for personal hire. It is best to check the hourly and daily rates charged by each hotel.

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\* Europcar  
Tel: +7 (3272) 581 681

### Interpreters

Even moderately fluent Russian speakers sometimes find an interpreter useful in business negotiations. It is also becoming more and more important to have an interpreter who speaks both Kazak and Russian and can interpret actions as well as words. Interpreters could be best arranged through the inviting organization, and cost between USD 50 and USD 150 per day.

### Appointments

Appointments are generally kept in Kazakhstan unless there is a good reason for breaking them. However, in the business climate in Kazakhstan, meetings can be frequently cancelled because other issues became even more urgent. Therefore, one should try not to schedule appointments more than two days in advance. If possible, confirm the appointment an hour before arrival.

## Working Hours

Standard working hours are nine to six, five days a week, with most people working a 40-hour week. Shops tend to be open later on weekdays and on Saturday, while most are also open on Sunday. Most offices and banks close for an hour or so during the day between one and two p.m. for lunch. Bazaars (baraholkas) are open every day from 9:00 a.m. until 5:00 p.m. except Mondays.

## Currency

Kazakhstan has a cash and, increasingly, a credit economy. Plan to have cash (Tenge) in the event that your credit card does not work at the restaurant or shop.

There are many foreign exchange points around, but it may be more reliable to use the banks or the hotels, where possible, since rates and security measures vary across the country. When changing money, worn or damaged bills must be avoided as most places accept only bills in good condition. US dollar bills, as well as the Euro bills, must be post-1990, ensuring that they have a metal strip encoded in them.

Automated teller machines (ATMs) can now be found in many places in Kazakhstan and especially in Almaty. ATMs typically dispense local currency and usually offer a reasonable exchange rate.

## Public Holidays

Before investing in a round-trip ticket to Almaty, it is prudent to be aware of the following official Kazakhstan public holidays:

January 1,2	New Year
March 8	International Women's Day
March 22	Nauryz (Central Asian New Year)
May 1	Day of Unity of the People of Kazakhstan
May 9	Victory Day
August 30	Constitution Day
October 25	Day of the Republic
December 16	Independence Day

Christmas and Easter are not public holidays in Kazakhstan. Also, please be aware that, where the holiday falls on Saturday/Sunday, typically the next Monday is a day off.

## Safety

In any city where disparities in income levels are large, crime tends to be targeted at the (comparatively) wealthy and Kazakhstan is no exception. Recently, Kazakhstan has been experiencing an increase in violent crime.

Foreign visitors are advised not to dress in a flamboyant fashion and to be discreet in their conduct. It is also recommended to drink in moderation and to exercise caution when leaving nightclubs and discos late at night. In particular, use known taxis or arrange for a hotel or company car to pick you up. Hotel safes should be used, where possible, to avoid carrying excess sums of cash.

Never walk alone, especially at night. If someone walks toward you, stops in front of you, and/or starts talking to you, do not stop. If somebody in front of you drops a wallet or anything valuable, do not pick it up or you may find yourself the target of a scam.

When staying in a hotel room or apartment, never open the door for anyone who is unfamiliar.

While in a car, always lock the doors as soon as you get in and keep windows closed even if temperatures are high. Avoid driving late at night, especially in deserted areas.

Always be alert in public places. If you are uncomfortable or suspicious of the situation, do not hesitate to alter your plans or route.

Almaty is no different from other big cities. If you are being robbed, do what they want. It is not worthwhile to be brave, risking injuries or worse while protecting your replaceable goods.

## Traditions

When invited by a Russian or Kazakh as a guest in their home, consider it an honor. Thus, it is impolite to decline the invitation. It is customary to bring something for the house and, if dinner will be served, (which is usually the case), something for the table. Shoes should be removed when entering the house. Greeting traditions, such as kissing each other or shaking hands, depend on the relationship with the host(s). If shaking hands, never shake hands over the doorstep.

Once seated at the dinner table, the host is likely to offer a glass with vodka and will give a toast in the guest's honor. The host is likely to toast to the health of everyone present, as well. All guests are expected to say a toast. The guest should stand, hold a glass of vodka (or alternative beverage) high, and speak to the host of the table. Something should be said in honor of the host and/or hostess, wishing long and happy lives with family and friendship, complementing Kazakhstan, then followed by 'Vashe zdarovje' and a sip, after which the speaker may sit down. 'Vashe zdarovje' means, in English, 'to your health'.

Stories abound about eating sheep heads and other pieces of meat to which many foreign individuals are not accustomed. These menus may not be offered in the larger cities, like Almaty, because the hosts are usually aware that the foreigners are not familiar with these dishes. In rural areas, though, anticipate a menu including the native Kazakh dishes.

## Languages

The language spoken in business and daily life is Russian, although Kazakh is heard outside of the major cities. However, the Government has decreed that the legal language is Kazakh. Increasingly, Kazakh is taught in schools and children's nurseries.

It may be helpful to learn some Russian or Kazakh words. Like many, the Kazakhstan people seem to appreciate it when foreigners show interest in their way of life and in communicating in the National (Kazakh) or common (Russian) language.

English	Russian	Kazakh
Hello!	Zdravstvuyte! / Privet!	Salemetsizbe / Assalam aleikum!
How do you do?	Kak dela?	Kalyniz kalay?
Good-bye!	Do svidanya! / Poka!	Sau bolyniz!
Thank you!	Spasibo!	Rakhmet!

## Attractions

Even though business in Kazakhstan can be time consuming, your schedule may allow you to see something of the city. Here are some ideas for Almaty:

### *Zelyony Bazaar*

Zelyony Bazaar means Green Market, called this since it is largely a food market with quality caviar from the Caspian region. Some traditional Kazakhstan souvenirs may be found. Bargaining is common in this region. Always be aware of potential pickpockets.

### *Panfilov Park*

Park is in downtown Almaty, near the Zelyony Bazaar. A memorial demonstrating a common Soviet design bears an eternal flame in commemoration of those who died during the Civil War of 1922-1924 and the Second World War. In the center of the park is the spectacular Cathedral. Built entirely out of wood, without nails, this cathedral survived a major earthquake at the beginning of the century. The Russian Orthodox Church restored the cathedral in the early 1990's.

### *Medeo*

This is the world's most famous open-air skating rink on which 200(!) records were broken. Situated within thirty minutes of Almaty, one can enjoy the breathtaking views all year.

### *Kok-Tobe Needle*

Closer than Medeo, a television tower sits atop the hills to the east of Almaty. It has nice views and shashlyk (similar to kebabs) restaurants, with a gondola ride to and from.

## Education

The Almaty International School opened in September 1993 and offers education to pupils between three and fourteen years of age. This is the first school to be opened in Almaty specifically for foreign nationals. The instruction language is English.

In the fall of 1999, another international school names “Miras” opened. This institution, sponsored by the First Lady Mrs. Sara Nazarbaeva, is based on an international educational system, with some instruction in English.

Most recently, a Montessori school opened in Almaty.

There are also a number of state and private local schools with instruction in Russian. The standards can be high, but the number of expatriate children in such schools is small.

## Health Care

More often than not, a change in diet and partaking of the local custom, vodka, is the cause of stomach complaints in Kazakhstan. The treatment usually requires a few days for acclimation. Although Kazakhstan citizens may believe that water out of the tap is potable, it is not recommended. Bottled water and soft drinks are readily available at stores and kiosks.

While Kazakhstan is presently not known for any particular diseases, travelers planning to spend extended periods of time in the Republic should make sure that they are up to date with tetanus, rabies, hepatitis, polio, cholera, typhoid inoculations, and encephalitis vaccines. Even for short visits, it is strongly advisable to be appropriately vaccinated. Consult a doctor or a travel clinic before traveling to Kazakhstan, allowing time for vaccination series.

Foreigners are advised to bring ample supplies of required medications for their use in an emergency, as the medicine supply in Kazakhstan tends to differ from what foreigners are used to in their home countries.

To date, a couple of international medical centers have been set up in Almaty.

Interteach Clinic

Tel: 7 (3272) 582-332; 588-100

Fax: 7 (3272) 582-332

SOS Clinic

Tel: 7 (3272) 581-912

The clinics usually require a prepaid annual membership fee to provide medical service. Other services available in Almaty are usually considered questionable for emergency operations and other similar requirements. For extensive and detailed medical services, outside services should be sought through Moscow or other internationally operated emergency evacuation services.

## TAXATION

After a series of amendments to the April 1995 version of the Law "Concerning Taxes and Other Obligatory Payments to the Budget", Kazakhstan introduced a new Tax Code, effective from 1 January 2002, with the intention of improving Kazakhstan's tax legislation and changing those provisions that the Government viewed as out-dated or ambiguous from the previous tax legislation. Since then, amendments to the Tax Code have been introduced each subsequent year, including 2003 through 2006.

The format of the new Tax Code is vastly different from the previous tax laws, with 568 articles incorporated in the new version. No detailed instructions to assist taxpayers with tax compliance have been issued to accompany the new Tax Code, on the basis that the new Tax Code itself is intended to be self-explanatory with regard to interpretations of various topics previously explained in separate Instructions issued by the Ministry of State Revenues.

With few exceptions, the statutory income tax rate for Kazakhstan legal entities, branches of foreign legal entities, joint ventures and wholly foreign-owned legal entities is 30%. One of the few exceptions to the 30% corporate income tax rate is for those entities which registered and continue operating in a target region, called a special economic zone. Kazakhstan currently has four special economic zones: in Astana ("Astana, the New City"), in Aktau ("Aktau Sea Port"), in Almaty ("Park of Information Technology"), and in the Sairam district of South-Kazakhstan region ("Ontustik"). Taxpayers who register in one of the special economic zones should meet certain criteria established by the legislation to be eligible for tax benefits.

In addition to income tax, permanent establishments (permanent establishments include branches) of foreign legal entities are subject to 15% tax on their net profit. Similarly, Kazakhstan legal entities are subject to a dividend distribution withholding tax at a rate of 15%. In both cases, an international double tax treaty could reduce the 15% net profit / dividend withholding tax rates. Assuming a 30% corporate income tax rate and a 15% net profit tax rate, the effective tax rate for both foreign and Kazakhstan legal entities is 40.5%. Corporate residence is generally determined by the place of incorporation, in practice.

Income generated by the business activities of a permanent establishment in Kazakhstan is taxable under Kazakhstan legislation irrespective of where payments are received. Kazakhstan residents (Kazakhstan legal entities, as well as individuals meeting the residency test) are taxed on their worldwide income. Non-residents are taxed on their Kazakhstan source income.

### Corporate Taxation

Taxable income is calculated based on aggregate annual income from activities, less total allowable deductions for the reporting period.

### Inventory

Inventory valuation is currently based on procedures established in the Kazakhstan Accounting Standards.

## Dividends

Dividend payments made by Kazakhstan legal entities are subject to a 15% tax withheld at the source of payment.

Branches of foreign legal entities are subject to a net profit tax of 15%. The principal difference between the dividend withholding tax and the branch net profit tax is that the dividend tax is due when dividends are paid. The net profit tax for branches is paid annually on net profit, calculated as taxable income less corporate income tax.

## Capital Gains

Capital gains are taxed as regular income, with the exception of the following capital gains which are currently not taxed:

- Capital gains from sale of shares listed as "A" or "B" shares on the Kazakhstan securities exchange (effective up to 1 January 2007);
- Capital gains from public sale of shares and bonds listed on the highest or next to the highest listing category on the Kazakhstan securities exchange (effective from 1 January 2007);
- Capital gains from sale of government securities and agency obligations;
- The price received by an issuer upon share placement in excess of par value.

## Transfer Pricing

Income also includes adjustments to prices under the Law on the State Control over Transfer Pricing, which took force in January 2001. Under this Law, both the customs and tax bodies have the authority to adjust prices to market and to assess penalties and fines together with additional taxes and customs payments. The following international transactions are subject to "control":

- Between interdependent and interrelated parties;
- Barter transactions;
- Executed via offsetting of claim;
- Concluded with entities (or persons) either registered in or which have bank accounts in countries with preferential tax regimes;
- With entities operating under a tax regime that differs from legislation;
- With an entity which has reported losses on its tax returns for two years preceding the year of the transaction;
- Anytime the price deviates from the market price by more than 10%.



## Foreign Income

Branches of foreign entities are generally subject to taxation in Kazakhstan on their Kazakhstan source income. Broadly, Kazakhstan source income is determined by the location of the operations rather than where payment was received.

Management, consultancy, financial, legal, auditing, and software maintenance and support services are characterized under current Kazakhstan tax legislation as Kazakhstan source income regardless of where the services are performed. From 1 January 2006, Kazakhstan source income also includes income earned from services carried out by entities resident in tax haven countries, regardless of where the services are provided. Tax haven countries are defined in the Tax Code as those states with a tax rate not more than 1/3 of the tax rate in Kazakhstan.

The Kazakhstan permanent establishment or resident paying Kazakhstan source income to a non-registered non-resident or taking such expenses for deduction will be held responsible for remitting the relevant withholding tax, unless double tax treaty relief is available. However, to benefit from the double tax treaty provisions, the non-resident service provider will be required to follow certain established procedures requiring opening a special bank account and filing a treaty application form with the tax authorities (except for income in the form of royalty, interest and dividends, or income from offshore services, for which automatic exemption is available based on certificate of residence of the service provider, confirming its tax residence in the treaty state).

## Deductions

Deductions, or "costs associated with earning income" as described in the Tax Code, except for those costs that may be disallowed or limited under the Tax Code, should be deductible subject to certain requirements.

In Kazakhstan, deductions should be supported by documents confirming that they are associated with earning business income. The Tax Code does not define or illustrate the documentation that would be considered sufficient evidence to support a deduction. In practice, this usually includes contracts/agreements, original invoices, verification of payment, and sometimes acts of transfer/acceptance.

Tax depreciation is calculated using the declining balance method described in the Tax Code. Capitalized assets, except for buildings and certain other assets, are depreciated according to asset groups set out in the Tax Code. According to changes to the Tax Code effective from 1 January 2006, the allocation of fixed assets was simplified from 9 groups to 4 groups.

The Tax Code currently establishes the maximum allowable rates for each asset group. Taxpayers may, however, choose to depreciate asset groups for tax purposes using rates lower than the maximum rates set forth in the Tax Code, now ranging from 10% to 40% depending on the classification. As noted above, buildings and certain other assets are depreciated on an individual basis.

In the event that the residual value of an asset group at the end of the reporting period is less than 300 monthly calculation indices (approximately USD 2,530 for 2006, depending on currency exchange rates and the current monthly calculation index), the taxpayer has the right to recognize the residual value as a deduction.

Taxpayers also have the right to apply double depreciation rates in the first tax period for new fixed assets that are put into operation for the first time, provided these fixed assets are used for business operations (specifically, for earning aggregate annual income) for not less than three years. During the first tax period, these assets should be accounted for in separate asset group.

## Consolidation

Kazakhstan does not have consolidation provisions for tax purposes. The government retains the right to tax branches and representative offices of foreign legal entities as separate taxpayers. Income received by each partner in consortia and entities operating under general partnership agreements are assessed for taxation separately with respect to the individual participant's share and taxed at the participant level.

## Value Added Tax

The standard Value Added Tax (VAT) rate is 15%, applied to turnover derived from goods sold, work performed and services rendered, and taxable import into Kazakhstan, except for those items that are specifically exempt and those to which a zero rate applies.

Based on a proposal prepared by the Kazakhstan government, it is anticipated that the VAT rate will drop to 14% starting in 2007, and further to 13%-12% in 2008-2009, respectively.

Currently, Kazakhstan tax legislation determines whether VAT applies to a transaction by reference to a consumption-based supply of goods, work or services rather than whether the transaction physically occurred in Kazakhstan.

The Tax Code requires that an entity with taxable turnover exceeding 15,000 monthly calculating indices (approximately USD 126,000 for the 2006 monthly calculating index, depending on currency exchange rates) in the previous 12-month period, to register for VAT purposes.

A reporting period for VAT is generally a calendar month, except for those entities whose taxable turnover is below 1,000 monthly calculating indices (approximately USD 8,400 for the 2006 monthly calculating index, depending on currency exchange rates). Those below the 1,000 monthly calculating indices threshold will be required to report and pay VAT on a quarterly basis.

VAT paid on passenger vehicles and residential buildings is currently not available for offset against VAT paid. Instead, it is included in the cost of the asset and expensed through depreciation.

VAT on goods, work and services not related to the entrepreneurial activities of a taxpayer and VAT attributable to assets received free of charge (excluding imports) is also not available for offset.

Declarations should be submitted and VAT remitted to the tax authorities by the 15th of the month following the reporting period, whether the reporting period is a month or a quarter.

Imported items may be subject to VAT at the point of customs clearance. VAT on VAT-able imported goods is currently calculated at 15% of the customs value of goods, including freight and customs levies and taxes.

Goods exported outside the territory of Kazakhstan are generally zero-rated for VAT purposes. International agreements on VAT can restrict or amend the definition of export for VAT purposes and, therefore, an export to a country with which such an agreement is in force may or may not be a zero-rated export for Kazakhstan VAT purposes. Please consult your PricewaterhouseCoopers tax advisor for more details on zero-rated VAT.

## Individual Taxation

Individual income tax rates are based on graduated rates and brackets, which are generally revised annually. The minimum rate is currently 5% and the maximum rate is 20% (based on government proposal, a flat rate of 10% is expected to be introduced effective from 1 January 2007).

The maximum rate applies to annual gross income in excess of 600 times the annual calculation base (or approximately USD 60,440, depending on exchange rates). Kazakhstan provides for very few exemptions from taxable income, the most notable being obligatory pension contributions.

Kazakhstan residents, including foreign citizens who are residents of Kazakhstan for tax purposes, can be taxed on their worldwide income. Foreign citizens and Kazakhstan citizens who are not residents for tax purposes are taxed on their Kazakhstan source income.

An individual becomes a Kazakhstan tax resident if he/she spends more than 183 days in Kazakhstan in any 12-month period. In applying the 183 day rule, Kazakhstan introduced a look-back rule such that 1/3 of the days spent in Kazakhstan in the first preceding year, plus 1/6 of the days spent in Kazakhstan in the second preceding year are added to the number of days spent in Kazakhstan in the current year to determine whether the residency requirement is met.

## Gross Income

All direct and indirect income received through employment or related activities during a calendar year are considered taxable income, which is comprised of both income taxed and not taxed at the source of payment. This includes prizes, profit sharing, bonuses, taxes paid on behalf of an employee, employer-provided housing/utilities and any indirect benefits received, unless specifically exempted by legislation.

## Deductions

Individuals registered as entrepreneurs or those working under certain special tax regimes can generally deduct business expenses connected with generating income, provided the income and expenses are adequately documented.

The personal allowance in Kazakhstan is the equivalent of one minimum annual calculating base, or currently approximately USD 100. An equivalent amount may also be deductible for each dependent living with the taxpayer without a separate source of income. For a taxpayer to substantiate dependants, certain documentation should be made available to the tax authorities upon request. (Effective from 1 January 2007, it is expected that individual will be permitted to make only one personal allowance deduction, which will be increased to approximately USD 900 per annum based on current coefficients and exchange rates).

## Tax Credits

Where a Kazakhstan tax resident has paid foreign income tax on income received abroad, a tax credit may be permitted to the extent that the foreign tax does not exceed the recalculated amount using Kazakhstan tax rates.

## Withholding Tax

Kazakhstan source income of non-residents, not operating through Kazakhstan permanent establishments, is subject to Kazakhstan withholding tax. The definition of Kazakhstan source income currently includes income from any managerial, financial, consulting, legal, auditing, and software maintenance and support services income of a non-resident, irrespective of where such services are provided. Also the definition includes income from any services provided by a resident of a tax haven country, i.e. countries where the effective income tax rate is less than 1/3 of the Kazakhstan tax rate. The list of tax haven countries is approved by the government and includes low tax jurisdictions, such as the BVI, Cayman Islands, etc.

The Kazakhstan taxpayer paying the income is obliged to withhold income tax at the source of payment unless a Kazakhstan-approved double tax treaty application reduces the withholding tax to zero and is on file with the income payer. Income of a non-resident from offshore services may be reduced or exempted from Kazakhstan withholding tax based on a certificate of residence of the service provider, confirming its tax residence in the treaty state. (See more under International Conventions).

## International Conventions

The Tax Code provides for an automatic reduction in withholding tax on interest, dividends and royalties and automatic exemption for income from offshore services, subject to proof of tax residency by the income recipient, on the basis of double tax treaties in force when the income is paid.

The responsibility for proper application of automatic exemption and/or rate reduction is placed on the tax agent paying Kazakhstan source income to a non-resident. Failing the automatic provision can result in the collection of withholding taxes, fines for late payment and penalty interest. Please consult your PricewaterhouseCoopers advisor for more specific information about application of double tax treaty benefits.

Withholding Tax Rates Between Kazakhstan and Treaty Countries  
(The letters in parentheses refer to the notes below)

Recipient	Dividends	Interest	Royalties
Nontreaty	15	15	20
Treaty:			
Austria (1)	5/15 (d)	10	10
Azerbaijan	10	10	10
Belarus	15	10	15
Belgium	5/15 (d)	10	10
Bulgaria	10	10	10
Canada	5/15 (a)	10	10
China	10	10	10
Czech Republic	10	10	10
Estonia	5/15 (b)	10	15
France	5/15 (d)	10	10
Germany	5/15 (b)	10	10
Georgia	15	10	10
Hungary	5/15 (b)	10	10
India	10	10	10
Iran	5/15 (e)	10	10
Italy	5/15 (d)	10	10
Korea	5/15 (d)	10	10
Kyrgyzstan	10	10	10
Latvia	5/15 (b)	10	10
Lithuania	5/15 (b)	10	10
Moldova	10/15 (b)	10	10
Mongolia	10	10	10
The Netherlands	5/15 (a)	10	10
Norway	5/15 (d)	10	10
Pakistan	12,5/15 (a)	12,5	15
Poland	10/15 (c)	10	10
Romania	10	10	10
Russia	10	10	10
Sweden	5/15 (a)	10	10

Switzerland	5/15 (d)	10	10
Tajikistan	10/15 (f)	10	10
Turkey	10	10	10
Turkmenistan	10	10	10
Ukraine	5/15 (b)	10	10
United Kingdom	5/15 (a)	10	10
United States	5/15 (a)	10	10
Uzbekistan	10	10	10

Notes referring to the table above:

1. Treaty withholding tax rates applicable from 1 January 2007.
2. 5% (or 12.5% in case of Pakistan) if the recipient is a company controlling, directly or indirectly, at least 10% of the voting power of the company paying the dividends.
3. 5% (10% in case of Moldova) if the beneficial owner is a company that directly holds at least 25% of the capital of the paying company.
4. 10% if the recipient is a company holding at least 20% of the capital of the paying company.
5. 5% if the actual owner is a company (other than partnership), which owns not less than 10% of the capital of paying company.
6. 5% if the recipient is a company (other than partnership), which directly owns not less than 20% of the capital of paying company.
7. 10% if the actual owner is a legal entity, which owns not less than 30% of the authorized capital of the legal entity paying the dividends.

## OTHER TAXES

### Excise Tax

Excise duties apply to the sale and import of crude oil (including natural gas liquids), fuel (excluding aviation fuel), diesel fuel, spirits or alcoholic beverages, caviar, tobacco, cars and firearms. Excisable types of activities include gambling and the organization and conducting of lotteries.

The Kazakhstan Tax Code provides for ad valorem and fixed excise rates. The taxable base for ad valorem rates is the selling price (excluding excise and VAT), whereas fixed rates apply to the natural per unit value. In the case of import, ad valorem rates apply to the customs value. Excise duty rates vary and historically are subject to frequent changes.

Export of certain products may require that the exporter hold specific licenses. In some cases, depending on the character of the exported items and the decision of the customs body, a selective pre-shipment inspection may be carried out.

### Property Tax

The current property tax rate for legal entities is 1.0% of the value of fixed and intangible assets, excluding vehicles, land, fixed assets that are put into operation within the framework of investment contracts, as well as construction in progress. For individual entrepreneurs, the property tax rate is 0.5%.

### Transportation Tax

Transportation tax is paid annually and is generally calculated as a percentage of the monthly calculation base for each kilowatt of the vehicle's power.

The transportation rates vary from 1 to 117 monthly calculation indexes (currently 1,030 KZT), depending on the type and kilowatt power of the vehicle. Adjustments are also made for the number of years that the vehicle has been in service.

### Land Tax

Land tax is applied to individuals and legal entities owning or using land. The tax rate is contingent on the land's location, quality, and use. Local authorities have the latitude to increase or decrease the tax rates set forth under Kazakhstan tax legislation by as much as 50%.

## Social Taxes

In Kazakhstan, employers bear the expense of the social taxes for their employees. Employers, in this context, include Kazakhstan legal entities, foreign legal entities carrying out activities in Kazakhstan through a permanent establishment, branches and representative offices, as well as individuals engaged in entrepreneurial activities.

Social taxes are calculated based on total wages paid, which has been expanded to include both Kazakhstan and foreign citizens.

Social tax is calculated using a regressive rates scale, whereby the larger the employee's gross annual income the lower the applicable rate.

- The maximum Social Tax rate for Kazakhstan personnel is 20% with a decrease to 7% at a certain threshold amount of an employee's taxable income.
- The maximum Social Tax rate for expatriate office and management, technical and engineering personnel is from 11% to 5%.
- For other foreign workers – the maximum Social Tax rate is from 20% to 7%.

Effective from 1 January 2008, it is planned that Social Tax rates should be reduced by 30%, on average, to stimulate employers to increase salaries.

The taxable base for Social Tax is calculated separately according to the amount of each employee's taxable income, rather than on an aggregate basis. Social Tax is reduced by the amount of Social Insurance Contributions

Social taxes are generally payable monthly, not later than the fifteenth day of the following month (twentieth starting January 2007).

Reports on the social tax should be filed not later than the fifteenth day of the month following a reporting quarter (twentieth starting January 2007).

## Social Insurance Contributions

The amount of social tax payable to the budget is reduced by the amount of the obligatory social insurance contributions payable to the separate fund. The base for calculating Social Insurance Contributions is the employer's expenses paid to an employee for work performed and services rendered. For 2006, this amount is capped at KZT 92,000 per month (or USD 750 at the current KZT/USD exchange rate). The Obligatory Social Insurance Contributions rate established for 2006 is 2%. From 1 January 2007, the rate will be 3%. These Contributions are not applicable to expatriate employees who have work permits.

## Pension Fund

Obligatory Accumulated Pension Contributions are withheld and remitted by employers at a rate of 10% of the gross remuneration for each Kazakhstan citizen, subject to certain adjustments. The monthly amount of employment income subject to obligatory pension contributions is capped at 75 minimal monthly salary indices, currently totaling KZT 690,000 (or USD 5,625 at



the current KZT/USD exchange rate), and resulting in a maximum monthly pension contribution of KZT 69,000 per individual.

The amount of pension contribution should be transferred on behalf of each Kazakhstan citizen employed to the Accumulated Pension Funds as designated by the employee.

In the absence of a designated Accumulated Pension Fund, payments should be directed to the State Accumulated Pension Fund. Regardless of where the payment is forwarded, payments should be made monthly, generally not later than the fifteenth day of the following month.

## Tax Administration

The tax year for Kazakhstan tax purposes is the calendar year.

Tax liability estimations and advance payments are required by entities, individuals engaged in entrepreneurial activities, and employers hiring expatriate employees (if certain conditions are fulfilled), with few exceptions.

Annual tax declarations are due not later than the 31st of March in the year following the tax year-end. Payments of outstanding tax liabilities are due within 10 working days after the deadline for submitting the tax declaration.

From 1 January 2006, Kazakhstan adopted International Financial Reporting Standards as its accounting standards.

## Penalties and Fines

Penalty interest is applied to late tax payments at 2.5 times the official National Bank refinancing rate (currently 8.5%) of the unpaid tax for each day of delay.

The Administrative Violation Code of Kazakhstan determines the applicable fines for tax violations. Under the Administrative Violation Code, the tax authorities may assess the following fines:

- Failure to submit a tax statement within 90 days of the deadline – up to 100 monthly calculation indices (approximately USD 840 for the 2006 monthly calculating index, depending on currency exchange rates).
- Understatement of advance corporate income tax payments by more than 10% – 70% of the understated tax. (Starting from 1 January 2007, it is expected that for understatement by more than 20%, the fine will be 40% of the understated tax.)
- Understatement of tax liabilities, including withholding tax liabilities – 50% of the unpaid tax.

Note: this applies to understatements resulting from both inaccurate tax computations as well as to correct computations on an incorrect tax base.

- Understated current payments – 50% of the understated payment.

- Understatement of advance individual income tax payment by more than 10% understatement – 70% of the understated tax. (Starting from 1 January 2007, it is expected that for understatement by more than 20%, the fine will be 40% of the understated tax.)
- Failure to account for income, expenses and other objects of taxation - 10% of the value of unaccounted goods (work, services).
- Concealment of taxable items – 150% of the value of the concealed amount.

Because the administrative penalties and fines in effect at the moment that the violation occurred are typically applied to taxpayers, the current legislation on penalties and fines should be monitored by anyone doing business in Kazakhstan. In many cases, this applies even to those taxpayers operating under stabilized tax regimes.

## Subsurface Taxation

### *Tax Regime*

In general Kazakhstan tax legislation establishes two models of tax regimes for subsurface users. The first model allows the subsurface user to pay all taxes (and other mandatory payments) except for Kazakhstan production sharing and the "top off" tax.

The second model is designed for subsurface contracts with Production Sharing Agreements (PSAs) with the Republic of Kazakhstan. Under either model, equivalent taxes should be paid although the second model defines the applicable taxes.

In July 2005, the Kazakhstan Government introduced the law concerning PSAs for conducting petroleum operations in the Kazakhstan sector of the Caspian and Aral Seas. This law provides that production sharing terms and tax terms of offshore PSA contracts shall be set in accordance with current legislation.

### *Special Taxes*

All subsurface users are required to pay special taxes and other obligatory payments. These other obligatory payments include: signature and commercial discovery bonuses, royalties, excess profit tax, rent tax on exported crude oil, and/or production share.

Although the list of special payments and taxes applicable to subsurface users is the same, the economics of a project generally determine amounts of applicable bonuses.

Royalty rates are also established based on the economics of the project. When extracting more than one mineral under a single contract, royalties are established for each type of mineral. Generally, petroleum contracts apply a sliding-scale royalty based on production levels. Tax legislation effective from 2004 establishes the rate of royalty paid on oil from 2% to 6% depending on the volume of the produced oil reserves for each calendar year. Effective from 1 January 2005, royalties are excluded from the list of taxes payable under PSA model subsurface contracts.

Subsurface users, except for those operating under PSAs, are liable to pay excess profit tax on net income for a reporting period where the ratio of accumulated income to accumulated costs is higher than 1.2. Excess profit tax is based on a progressive sliding scale where the maximum tax rate of 60% applies to amounts exceeding the 1.7 ratio of accumulated income to accumulated costs.

A new tax was introduced starting from 1 January 2004: rent tax on exported crude oil and gas condensate applies to legal entities and individuals selling crude oil and gas condensate for export (except for subsurface users that concluded production sharing agreements). The taxable item for rent tax on exported crude oil is the volume of crude oil sold for export. Rent tax rates are determined by reference to the "market price" of exported crude oil and vary from 1% if the market price is USD 19 per barrel, to 33% if the market price exceeds USD 40 per barrel. This tax applies to oil traders as well as oil producers operating under Model 1 contracts.

## Production Sharing

The Tax Code sets out a detailed and complex mechanism for production sharing to be applied in Production Sharing Contracts (PSA) with the Government of Kazakhstan signed effective from 1 January 2004. The profit share of a contractor under a PSA is determined as the lowest of the following three triggers:

- R-factor (profit ratio) – ratio of accumulated net revenues to accumulated expenses;
- Internal Rate of Return (IRR), and;
- P-factor (price ratio) – ratio of net revenue to extracted volume of petroleum.

The minimum contractor's profit oil share is 10% and the maximum share is a negotiable 70-90%. Cost recovery is capped at 75% before payback and 50% after payback.

Additionally, the PSA regime envisages a "top off" tax which ensures that the government's take is above 5-10% before payback and is at least 40% after payback.

## Special Exemptions

Geological prospecting and geological exploration turnover, as well as assignment of geological rights, are VAT exempt. Kazakhstan tax legislation describes certain criteria that should be met to secure the VAT exemptions.

## Deductions

Exploration and development expenditures incurred by subsurface users prior to commercial production (including: geological studies, geological prospecting, exploration, appraisal and development of natural resources, general and administrative costs, signature and commercial discovery bonus payments, expenditures for the purchase of fixed and intangible assets, and other tax deductible expenses, except for mineral selling expenses) should be deductible from aggregate annual income through depreciation charges. These expenditures form a separate group with a maximum depreciation rate for tax purposes of 25%.

The same depreciation procedure applies to expenditures for the acquisition of intangible assets incurred by a subsurface user in relation to the acquisition of subsurface rights.

Administrative expenses to be recovered under a subsurface use contract in a reporting period cannot exceed 1% of the total recoverable expenses in that reporting period.

## Losses

Losses incurred from operations under subsurface use contracts may be carried forward for up to seven years.

## Ring Fencing

Ring fencing provisions apply to prevent multiple contract areas from being combined for the purposes of applying the tax regime under a subsurface use contract.

## Stability of Tax Regime

Kazakhstan legislation permits tax regimes to be stabilized under those contracts with the government that were concluded prior to 1 January 2004 and subjected to expert tax inspection by appropriate government departments. Tax provisions stipulated in PSAs concluded before and after 1 January 2004 may also be stabilized. However, a tax regime can be amended with the mutual consent of the parties. Under the Tax Code, a tax regime may be modified if the subsurface user's position improves so that the economic interest of the State may be restored.

With respect to Tax/Royalty contracts entered into force after 1 January 2004, stability guarantees may not apply and the tax regime should adhere to the legislation in force at the time the obligation arises.

## CUSTOMS

### Customs Code

With effect from 1 May 2003, Kazakhstan introduced a Customs Code. The Customs Code cancels the provisions of the Law "Concerning the Customs Business in the Republic of Kazakhstan" dated 20 July 1995. However, according to the Customs Code privileges provided under previously concluded investment contracts will remain valid until the termination date stipulated in these contracts.

### Exports

Exports of goods are generally not subject to export customs duties, with certain exceptions noted (e.g., aluminum, iron-scrap, copper-scrap, certain petroleum products, etc.).

### Imports

Customs duties are established either as a percentage of the customs value of imported goods, or as a fixed rate (e.g., euro per liter) with respect to certain unit (sometimes, combined rates apply). The import customs duties are subject to revision by the Government.

### Customs Fees

The Customs value is generally determined by the declared value of goods plus transportation and insurance-related expenses. The levy, or fee, for customs processing is generally EURO 50 for the main page of the customs declaration and EURO 20 for each additional page.

### Customs Clearance

Goods and transport vehicles may be declared either by Kazakhstan legal entities or individuals (both Kazakhstan nationals and foreign) moving these goods and vehicles or a licensed customs broker. Branches and representative offices of foreign legal entities need to engage the services of a brokerage firm to release their goods.

## PETROLEUM TAXATION

### Introduction

During the Communist period, decisions affecting every aspect of Kazakhstan's economy were made in Moscow. As a result, development within the Republic of Kazakhstan was often stimulated by the needs of other parts of the USSR. This is exemplified by the presence of oil refineries, metals smelters and processing plants, which were designed to process materials from other republics rather than from Kazakhstan.

Historically, several problems have been identified in the Kazakhstan hydrocarbon infrastructure, most of which involve its technical capabilities. As a result, Kazakhstan's oil industry depends heavily on other CIS republics, and particularly Russia, for its operational capabilities, including the ability to maintain and provide spare parts for the production facilities and pipelines. Problems in Kazakhstan's infrastructure have historically included a lack of spare parts for pipeline and drilling equipment, an inability to operate existing oil fields, an inability to explore and develop oil wells, the use of Russian technology not compatible with Western technology, and noticeably low oil production efficiencies.

Recent years have considerably reduced the impact of these problems with the increased interest by western companies in Caspian resources. Although the fluctuating level of worldwide oil prices dampened this interest in the latter part of 1998, most large western oil companies consider their investment in Kazakhstan long-term and have not significantly decreased their initial investment projections.

Indeed, as the recent ripple effect on Kazakhstan's economy will attest, Russia will continue to exert influence on oil development and expansion activities in Kazakhstan for years to come because of Kazakhstan's landlocked position and its continued reliance on Russia for a variety of natural resources and consumer goods. The other Central Asian republics also depend largely on Russia for energy supplies and will, no doubt, closely monitor the future direction of the Kazakhstan oil industry as an indication of their options for the future.

Kazakhstan's oil production is concentrated in the West, and two export pipelines transport this oil to refineries and export pipelines in Russia. However, Kazakhstan's urban and industrial centers are concentrated in the East, and because they are not connected to the production centers, they import oil via an oil pipeline from Siberia. As a result, Kazakhstan's pipeline system is fragmented, consisting of the two export pipelines in the West, the import pipeline in the East, and a smaller internal line in the South. At the same time, Kazakhstan is now trying to find alternative export route that should allow the export of oil through Turkey and China.

China has increased its state in the Kazakhstan part of Caspian oil reserves to support its booming economy. As a result, in 2006, Kazakhstan-China Pipeline has finished the construction of Atasu-Alashankou pipeline which has a full capacity of 400,000 barrels a day. It is expected that a sixth of Kazakhstan's total oil production would be routed through this pipeline to China.

Kazakhstan should also be able to export oil through Baku-Tbilisi-Ceyhan pipelines after its construction. If the Kazakhstan government can facilitate new pipeline development or major refurbishment of the existing system, and if western companies continue to fund investment in Kazakhstan to increase shareholder value, the country may become one of the most attractive in the world for foreign investment and technological assistance in the oil industry.

## Industry Overview

Kazakhstan is one of the most promising and problematic of the world's petroleum provinces that remain to be developed. Kazakhstan's development is problematic from an operational perspective since it is landlocked. For its oil to reach international markets on a regular basis, Kazakh oil must be piped either through control-seeking Russia to the Black Sea, unpredictable Iran to the Persian Gulf, or the unsettled Caucasus to reach Turkey. Other, less practical, routes have been considered through Uzbekistan and Afghanistan or through China to Pakistan and the Indian Ocean. All of these projects have two common characteristics: they are expensive and time-consuming.

Following this is the question of the political stability in Kazakhstan or, more precisely, the legal stability. While President Nazarbaev firmly controls the political process in Kazakhstan, there is still much public debate over how resources should be developed and what price the government should exact for them. Economic growth in recent years has been propelled by Kazakhstan's growing petroleum industry, and as a result, the state's budget revenue is roughly 50% dependent on the oil sector. Several economic research efforts conducted in 2002 and 2003 highlighted the growing danger of possible over-reliance on the oil sector, with some analysts predicting that without more investment into the country's non-oil sectors, Kazakhstan's economic capacity will be strained by 2007, thus stifling growth in the next decade. Since Kazakhstan is in need of capital in every sector of its economy and public infrastructure, taxes, royalties, and bonuses on petroleum operations can be oppressively high for some foreign investors, particularly when an investor is contemplating an expensive development in the offshore Caspian - one of the harshest and most challenging of known oil and gas deposits.

Meanwhile, the Kazakhstan Government adopted an aggressive approach toward oil & gas activities conducted by private companies, including foreign investors, whereby such companies are becoming extensively subject to various controls by tax and customs authorities.

It seems that the Republic now seeks to obtain interest in major oil and gas projects through KazMunaiGas. Recently, the Government (KazMunaiGas in practice) was granted a priority right to purchase interest in the oil & gas projects if sold by one of the project members. One example of exercising this right is the purchase of 50% of the British Gas share in the North Caspian project (Kashagan) that took place in Spring 2005. Moreover, the Law on PSAs for Sea Operations, now in force, allows the Republic to introduce amendments to PSAs, and also gives KazMunaiGas the right for at least a 50% stake in any offshore oil and gas project. This right can be exercised at any stage of the project, which would allow Government to enter the projects after the risky exploration stage.

In addition, following the trend now visible in Russia, Kazakhstan is now making its local content requirements more demanding and more restrictive while insisting upon the introduction of modern technology by foreign investors. Local content is especially relevant during tenders for the new projects, where the availability of new technology combined with ample use of local goods and services can earn additional points for the bidder.

## National Oil & Gas Company

In 2002, the former national oil company, KazakhOil, and the national oil transportation company, KazTransOil, were combined into one entity, KazMunaiGas, which now owns the domestic pipeline system, providing transportation through Kazakhstan for oil producers.

KazMunaiGas is overseen by the Kazakhstan Ministry of Energy and Natural Resources, and its primary function is to represent the State's interest in organizations engaged in hydrocarbon exploration, production, transportation, and refining as well as in production sharing agreements. KazMunaiGas is participating in tenders for hydrocarbon exploration and production contracts on behalf of the government as well as handling the marketing and sale of hydrocarbons on behalf of the State.

Recent changes in the legislation, and changes that are being introduced now, significantly increased KazMunaiGas' role. For example, according to the recently introduced Law on PSAs for Sea Operations, KazMunaiGas has the right for at least a 50% participation in any project undertaken in Caspian or Aral Sea.

## Oil Prices

Average export prices from Kazakhstan to countries outside of the CIS do not differ significantly from the world crude oil market. However, average domestic prices in Kazakhstan are below the world market. Average exports prices to CIS countries lie in-between the domestic price and the export price but are becoming more consistent with Kazakhstan domestic prices.

## Transportation

The current export pipeline capacity of Kazakhstan is limited with the majority of pipelines passing through the Russian Federation. The Kazakhstan government and producers are, however, seeking alternative routes in an attempt to increase capacity and to reduce the dependency on Russia. This is currently being accomplished via the Baku-Tbilisi-Ceyhan and Atasu-Alashankou pipelines.

The existing domestic oil and gas pipelines deliver Kazakhstan crude to one of three Kazakhstan refineries or to southern Russian refineries. They also deliver natural gas from Uzbekistan to cosmopolitan centers.

Other modes of oil transportation used in Kazakhstan typically include rail cars, trucks, and barges.

## Pipeline Tariffs

Tariffs for the transportation of hydrocarbons in Kazakhstan are set by KazTransOil, and approved by the Agency of the Republic of Kazakhstan for the Regulation of Natural Monopolies and the Protection of Competition. The tariffs in Kazakhstan for oil and gas transportation principally depend upon three factors: logistics costs, tariffs for power energy, and the interest rate on bank credits. Significant changes in any of these factors will cause fluctuations in the tariffs.



## Refineries

There are three refineries in Kazakhstan: the Shymkent refinery in the south, primarily servicing the Kumkol field; the Atyrau refinery in the northwest, servicing the Tengiz and other western fields; and Pavlodar in the northeast, handling mostly Russian crude. Last year these refineries processed over 10 million tons of hydrocarbons. Moreover, domestic production of gasoline and diesel has increased over the last couple of years, and the Pavlodar and the Atyrau refinery underwent substantial upgrades in 2006.

## Licensing

Operations related to subsurface use were previously subject to licensing. Obtaining the license was a precondition for negotiating provisions of the future Subsurface Use Contract with the Government. However, the 1999 amendments to the Law Concerning the Subsurface and Its Use removed the licensing requirement. Consequently, the procedures for amending existing licenses typically include obtaining a Prime Minister's decree, which often delays the negotiation of the contract. (Note, this is relevant for companies farming into an existing project.)

## Petroleum Regulations

Currently, the Law on Subsurface and Its Use and the Petroleum Law are the key documents establishing the fundamentals for petroleum exploration and production in Kazakhstan. The basis for any operation related to subsurface use is a subsurface use contract, concluded between a subsurface user and the State, who is generally represented by the appropriate State body. Production Sharing Agreements (PSAs) and Tax/Royalty Contracts are the two kinds of contracts currently offered in Kazakhstan with the tax/royalty being the most common.

To create a legal basis for PSAs concluded for development of oilfields in the Caspian and Aral seas, the Kazakhstan Government introduced the Law on PSAs for Sea Operations. This law establishes the maximum periods for PSAs, which is: 35 years for exploration and production PSAs; 25 years for production PSAs; and 45 years for PSAs with unique reserves. Other notable provisions of the law include: KazMunaiGas' right to not less than a 50% participatory interest in any project, tender procedures, mandatory participation of the Kazakhstan side in combined oil development and production works, obligations to refine a certain portion of crude oil in Kazakhstan, and criteria regarding the bid winner's ability to develop existing technology in or bring new technology.

Under these individually negotiated PSAs, the laws and tax policy existing at the effective date of the contract (usually the date of registration with the Government) are "frozen", thus stabilizing the tax regime for a set period of time. An essential element in the effective use of the provisions of PSAs is the development, agreement, and use of detailed implementing agreements, particularly where the contract itself does not elaborate on particular details of tax accounting and computation. Stability of tax regimes remains a key issue and one to which subsurface users are advised to pay close attention.

## PSAs

Due to frequent changes in the Kazakhstan tax legislation, Kazakhstan taxpayers are uncertain as to the fiscal regime to which they will be subject. However, Kazakhstan legislation, including supporting provisions in the Foreign Investment Law and the Tax Code, allow for stabilization of the tax regime applicable to a subsurface user operating under a PSA. As such, the Company's tax regime is "frozen" at the time of signing its PSA with the government and subsequent amendments to the tax laws should not be permitted to worsen the Company's tax position.

Effective from 1 January 2004, the statutory limit to the tax obligations of subsurface users are increased from five years following a tax period, to five years after the termination of the subsurface contract.

Assurances can sometimes be made regarding the specifics of the tax regime applicable to a subsurface user through preparation and negotiation of contract-like directives for tax purposes. These directives serve as the basis for the calculation and payment of all tax obligations applicable to the subsurface user.

Amendments to a tax regime under a subsurface use contract, which do not entail any alterations in the original economic interest of Kazakhstan and the subsurface user, are allowed under the Tax Code, subject to certain conditions and agreement of the parties. Under the current Tax Code, however, any improvements to the subsurface user's position will result in amendments to the subsurface contract to restore the Government's economic interest.

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