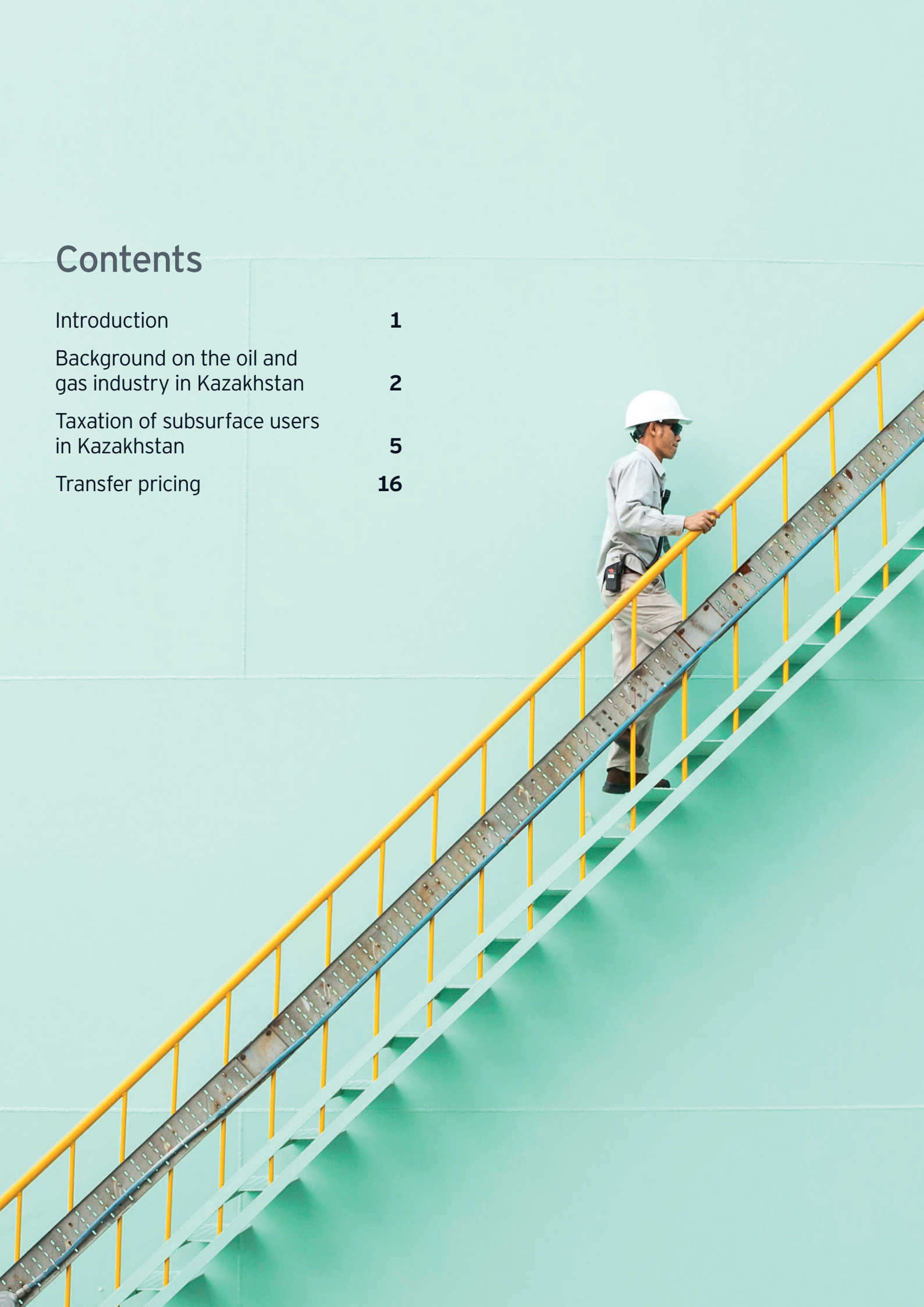
Kazakhstan oil and gas tax guide

2021

EY

Building a better working world

Contents



Introduction

This guide is intended to provide a general overview of taxation in the oil and gas sector in Kazakhstan.

As this guide provides a high-level summary of the taxation regime effective on the date of preparation of this guide, it is not a substitute for comprehensive professional advice, which should be sought before engaging in any transaction. It should also be noted that in this guide we do not deal with all of the taxes of Kazakhstan. Here we cover only the most significant ones applicable to companies operating in the oil and gas sector, so advice should be taken as to the actual taxes applicable to a particular company.

Background on the oil and gas industry in Kazakhstan

The oil and gas industry of Kazakhstan plays an important role in the economic development of the republic. It is one of the main drivers of gross domestic product (GDP) growth and an important source of national budget revenue.

According to the latest GDP forecast by the Ministry of National Economy of Kazakhstan, growth in 2021 will be 2.8%. Kazakhstan's economic growth is largely driven by oil and gas revenues (35% of GDP and 75% of exports).

Since declaring independence, Kazakhstan has passed a series of reforms to liberalize its economy and attract foreign investment. However, sanctions imposed on Russia and negative growth prospects have more recently deterred foreigners from investing in the region. According to UNCTAD's World Investment Report 2020, FDI inflows to the country totalled US$ 3.1 billion in 2019, a slight decrease from the previous year (US$ 3.8 billion). Total FDI stock stood at US$ 150 billion in 2019. The country remains the 2nd-largest recipient of FDI in the region, behind Russia. The oil industry and metallurgy are the main sources attracting FDI to the country.

According to BP's Statistical Review of World Energy 2020, Kazakhstan has proven oil reserves estimated at 30.0 billion barrels (3.9 billion tons) and proven natural gas reserves of 93.7 trillion cubic feet (2.7 trillion cubic meters), which account for 1.7% and 1.3% of total global reserves, respectively.

Kazakhstan is the 2nd-largest oil producer among the former Soviet republics after Russia and is heavily reliant on oil export revenues. Total production of oil and gas condensate in 2019 amounted to 91.4 million tons, up 0.2% year on year.

In April, Kazakhstan assumed new obligations under the agreement between the OPEC+ countries to collectively cut oil production by 9.7 million barrels per day in May – July 2020. In accordance with the agreement, Kazakhstan's maximum allowed output for July amounted to 1.319 million barrels per day. The government of Kazakhstan expects total oil production in 2021 to amount to 86 million tons, with an increase by 2025 to 100.7 million tons.

State participation in the oil and gas industry has increased over the last few years due to the vital role of this industry in the economy of the republic. The main production of hydrocarbons in Kazakhstan is concentrated in the three largest fields: Tengiz, Karachaganak and Kashagan, the development of which is carried out by established consortia with the participation of transnational vertically integrated companies. The vertically integrated National Company KazMunayGas represents the state's interests in the industry. The company controls 26% of total proved oil and gas reserves of Kazakhstan.

Oil production

Currently, there are 172 oil and 42 gas condensate fields registered in Kazakhstan, including 80 that are being developed. More than 90% of the total reserves of Kazakhstan are concentrated in the 15 largest fields: Tengiz, Kashagan, Karachaganak, Uzen, Zhetybai, Zhanazhol, Kalamkas, Kenkiyak, Karazhanbas, Kumkol, North Buzachi, Alibekmola, Central and Eastern Prorva, Kenbai and Korolevskoye.

Tengiz field

The Tengiz field was discovered in 1979. Its recoverable crude oil reserves are estimated at 750 million to 1.1 billion tons (6–9 billion barrels). The Tengizchevroil (TCO) partnership has been developing the Tengiz field since 1993.

Tengizchevroil ownership structure

Owners	Equity share
Chevron (US)	50%
ExxonMobil (US)	25%
KazMunayGas NC (Kazakhstan)	20%
LUKArco (Russia)	5%

In 2020, TCO produced 24.3 million tons of oil over the first 11 months, which is 18% less than in the same period of the previous year (28.7 million tons). The forecast for oil production in Kazakhstan for 2021 has already been revised taking into account new circumstances. The production cuts scenario is still being worked out by the Ministry of Energy of the Republic of Kazakhstan.

Kashagan field

Kashagan, the largest offshore field within the North Caspian PSA contract area, was discovered in 2000. Its proved recoverable oil reserves equal 761.1 million tons. Kashagan's owners will continue to explore other structures in the North Caspian PSA contract area – Kalamkas-Sea, South West Kashagan, Aktoty and Kairan. The North Caspian Operating Company (NCOC), a company owned by both foreign and local investors, is the current operator of the project. In 2019, NCOC successfully completed the first turnaround of its onshore and offshore facilities and reached a production rate of 380,000 barrels per day.

North Caspian Operating Company ownership structure, 2020

Owners	Equity share
KazMunayGas NC (Kazakhstan)	16.88%
Eni (Italy)	16.81%
ExxonMobil (US)	16.81%
Royal Dutch Shell (Netherlands/UK)	16.81%
Total (France)	16.81%
CNPC (China)	8.33%
INPEX (Japan)	7.56%

In 2020, the volume of oil production at NCOC was 13.9 million tons, meaning that the plan for January-November was 100% fulfilled, but was down 2% versus 2019.

Karachaganak field

The Karachaganak field, which is being developed by Karachaganak Petroleum Operating B.V. (KPO), a joint venture between several Western companies led by BG Group and Eni, has estimated recoverable reserves of 9 billion barrels (1.2 billion tons) of oil and gas condensate, as well as 1.35 trillion cubic meters of natural gas reserves. The company produced 10.2 million tons of oil in 2012. In 2012, KazMunayGas NC joined the project, acquiring a 10% stake from its current shareholders. Karachaganak was for a long time the last large oil and gas project in Kazakhstan without the state's participation.

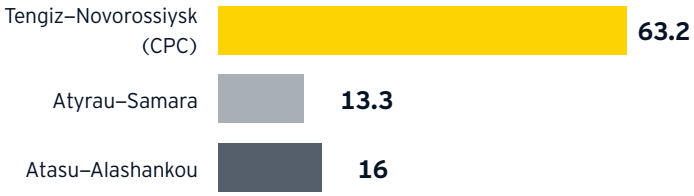
KPO ownership structure 2020

Owners	Equity share
BG Group (UK)	29.25%
Eni (Italy)	29.25%
Chevron (US)	18.0%
Lukoil (Russia)	13.5%
KazMunayGas NC (Kazakhstan)	10.0%

Oil export routes

Kazakhstan is a landlocked country. Consequently, transportation costs are high and the lack of export routes presents a potential bottleneck for Kazakhstan's ambitious development plans. Oil is exported via the Caspian Sea, rail cars and pipelines. Currently, the largest offtake routes are as follows:

Route volume of exported oil in 2019, million tons



Expansion of export routes

Given the oil production growth plans for the three main oil and gas projects – Kashagan, Tengiz and Karachaganak – Kazakhstan is working on expanding oil export routes to Europe and China.

Tengiz–Novorossiysk (Caspian Pipeline Consortium)

The CPC pipeline, with a total length of 1,510 kilometers, connects the Tengiz oil field with an oil terminal in Novorossiysk, Russia's port on the Black Sea coast. In 2018, the CPC Marine Terminal, which since the very beginning has operated like clockwork, was once again an award winner in the following categories: Grand Prix, Environmental Safety and Transshipment Giants.

Kazakhstan–China pipeline

The Kazakhstan–China pipeline is being constructed in two phases. Phase 1, the Atasu–Alashankou oil pipeline, with annual capacity of about 10 million tons a year, began operation in July 2006. Kazakhstan shipped 7.5 billion cubic meters (bcm) of gas to China in 2019 and plans to gradually increase shipments to 10 bcm a year.

Oil refining in Kazakhstan

Kazakhstan has three major oil refineries supplying the northern region (at Pavlodar), western region (at Atyrau) and southern region (at Shymkent). The refinery at Pavlodar is supplied by West Siberian crude oil with a likelihood of being substituted with Kazakh oil; the Atyrau refinery runs solely on domestic crude from northwest Kazakhstan, while the Shymkent refinery currently processes oil mostly from the field at Kumkol. The global pandemic did not significantly affect KMG's refining sector in the first quarter of 2020. However, lockdown measures in Kazakhstan's major cities have resulted in a decrease in energy consumption and an adverse effect on the refineries' operations. Refineries continue to operate; however, to avoid oversupply, both Pavlodar and Shymkent refineries are operating at minimal balanced capacity. Starting from mid-March 2020, Kazakhstani refineries' production has been reduced by around 13%. Refining volumes of Kazakh refineries (net to KMG) slightly increased and amounted to 3,348 thousand tonnes. The growth was at Atyrau refinery to balance production of oil products in the country due to declining volumes at Pavlodar and Shymkent refineries. A slight decrease at Pavlodar and Shymkent refineries was observed on the back of oil quality issues at CNPC AktobeMunaiGas in January and lockdown measures in Kazakhstan's major cities, leading to lower oil products consumption.

Gas industry in Kazakhstan

According to BP's Statistical Review of World Energy 2020, Kazakhstan has proven natural gas reserves of 93.7 trillion cubic feet (2.7 trillion cubic meters). Most of Kazakhstan's natural gas reserves are located in the west of the country, with roughly 49% of proven reserves situated in one field, Karachaganak. In January-May 2020, production of natural gas reached 24.8 billion cubic meters – 7.2% more than in the same period of 2019.

Taxation of subsurface users in Kazakhstan[1]

This section describes the tax legislation applicable to oil and gas companies.

Subsurface use legislation

Two major legislative acts in Kazakhstan govern the economic terms established in a subsurface use contract. They are the Subsurface Use Code[2], which contains the basic legal framework for granting, using and assigning or terminating rights to be a subsurface user, and the Tax Code3, which is discussed in detail below.

Stability of the tax regime

There are two types of subsurface use contracts in Kazakhstan: a production sharing agreement (PSA) and an excess profit tax (EPT) contract.

The tax regimes of the small number of PSAs concluded prior to 2009 are stable provided that they have undergone a "tax expert evaluation".

The tax regimes of EPT contracts are not stabilized except for cases where such contracts are approved by the President of the Republic of Kazakhstan.

Stabilized contracts can be changed by mutual agreement between the parties.

Ring-fencing

The tax regime of a subsurface use contract applies to activities that are carried out within the framework of the contract and that meet the definition of subsurface use in the Subsurface Use Code. The Tax Code implies that the tax boundary occurs after the extraction and primary processing stages.

Statutory and tax accounting

The Tax Code contains detailed requirements for tax policy and a set of tax registers that provide the bridge from the underlying accounting records to the tax returns.

Statutory accounting records are maintained in accordance with the Law on Accounting and Financial Reporting, under which most companies should prepare financial statements under International Financial Reporting Standards (IFRS).

[1] Oil, gas and mining companies in Kazakhstan are referred to as "subsurface users" and enter into "subsurface use contracts" to acquire the rights to exploit the mineral resources of the country.

[2] Code No. 125-VI of the Republic of Kazakhstan On Subsurface and Subsurface Use dated 27 December 2017.

[3] Code No. 120-VI of the Republic of Kazakhstan On Taxes and Other Obligatory Payments to the Budget dated 25 December 2017.

Taxes applicable to subsurface users

A. At a glance

Fiscal regime

This section describes the fiscal regime in force for almost all existing subsurface use companies in the petroleum industry. This regime is applicable to all contracts except PSAs that came into effect prior to 1 January 2009 and contracts approved by the President of the Republic of Kazakhstan.

The generally established fiscal regime that applies in Kazakhstan to exploration and production contracts in the petroleum industry consists of a combination of corporate income tax, rent tax on exports, bonuses, mineral extraction tax and other taxes of subsurface users. Oil and gas production activities are ring-fenced from downstream activities and from each other (i.e. contract by contract) for tax purposes.

Mineral extraction tax

Mineral extraction tax (MET) is a volume-based royalty-type tax applicable to oil, crude and associated gas. Different rates apply, depending on what is produced and whether it is exported, sold domestically or used for own production needs.

Signature bonus

Subsurface users are expected to pay a signature bonus.

Corporate income tax (CIT)

CIT is applied to all companies at a rate of 20% of taxable income.

Rent tax on exports

The tax base is determined as the value of the exported crude oil and crude oil products, including gas condensate, based on the same tax valuation as for MET. The tax rate ranges from 7% to 32% and is applied once the notional world prices for crude oil and crude oil products exceed US$50 per barrel.

Excess profit tax (EPT)

EPT is calculated annually. The tax is paid at progressive rates applicable to the portion of net income that exceeds 25% of deductions. The taxable tranches are derived by applying percentages of the deductible expenses.

Alternative Subsurface Use Tax (ASUT)

ASUT was introduced on 1 January 2018. ASUT may be applied by the subsurface user as a substitute for payment for compensation of historical costs, MET and EPT (at the discretion of the subsurface user). ASUT may be applied only by the subsurface users carrying out hydrocarbons production on the continental shelf or certain deep oilfield deposits.

Capital allowances

The value of fixed assets is deductible by means of depreciation charges for CIT and EPT purposes.

Carry forward of losses

Tax losses relating to subsurface use contracts can be carried forward for up to 10 years for the purpose of offsetting them against taxable income of the respective tax period.

B. Fiscal regime

The taxes applicable to subsurface users are as follows:

Applicable taxes	Rate
Bonuses	Variable
Mineral extraction tax	For oil – 5% to 18%; for gas – 10%
Excess profit tax	0% to 60%
Payment for compensation of historical costs	Variable
Alternative subsurface use tax	0% to 30%
Rent tax on exports	0% to 32%[4]
Excise on crude oil and gas condensate	KZT 0 per ton
Land tax	Generally immaterial
Property tax	1.5%
Environmental fees	Variable
Other fees (e.g., fee for the use of radio frequency spectrum, fee for the use of navigable waterways)	Variable
Other taxes and payments	Variable
VAT	12%
Crude oil export duty	Variable

EPT

EPT is calculated annually. The taxable amount is the portion of net income (if any) that exceeds 25% of deductions. Taxable income is calculated as aggregate annual income less deductions less CIT and branch profits tax, if any. For EPT purposes, deductions are the expenditure deductible for CIT purposes (with some adjustments). The tax is calculated by applying the following rates to the tranches of excess income, each tranche being allocated the marginal net income determined as a percentage of deductions until total net income is allocated.

[4] Zero percent tax rate if the world price for crude oil and crude oil products is less than US$50 per barrel.

Net income allocation schedule for EPT, % of deductions	% for calculating marginal net income allocation for EPT	EPT rate (%)
Less than or equal to 25%	25	Not set
From 25% to 30% inclusive	5	10
From 30% to 40% inclusive	10	20
From 40% to 50% inclusive	10	30
From 50% to 60% inclusive	10	40
From 60% to 70% inclusive	10	50
Over 70%	Any excess	60

Payment for compensation of historical costs

The payment for compensation of historical costs is a fixed payment by the subsurface user to compensate the state for geological survey and development costs of the contract territory and exploration of the oilfield deposits incurred before the subsurface use contract was concluded.

The obligation to compensate for historical costs arises from the date when the confidentiality agreement is concluded between the subsurface user and the authorized state body on subsurface study and usage.

MET

MET applies to oil, crude and associated gas. The taxable base is the value of the production. For export sales, the value is based on world prices without adjustments.

The world price of oil, crude and associated gas in this context is determined as the arithmetic mean of daily quotations for each of the Urals Mediterranean (Urals Med) or Dated Brent (Brent Dtd) brands in the tax period on the basis of information published in *Platts Crude Oil Marketwire*.[5] If that source does not provide price information for those brands, the source Argus Crude should be used.[6]

The world price for gas is determined as the arithmetic mean of daily quotations for Zeebrugge Day-Ahead in the tax period on the basis of information published in *Platts European Gas Daily*[7]. If that source does not provide price information for natural gas, the source *Argus European Natural Gas*[8] should be used.

The rates of tax are determined by the annual volume of production. The tax rates for oil are provided below.

Annual production of oil for each calendar year (thousand tons)	MET rate (%)
Up to 250 inclusive	5
Up to 500 inclusive	7
Up to 1,000 inclusive	8
Up to 2,000 inclusive	9
Up to 3,000 inclusive	10
Up to 4,000 inclusive	11
Up to 5,000 inclusive	12
Up to 7,000 inclusive	13
Up to 10,000 inclusive	15
Over 10,000	18

These rates are reduced by 50% if the production is processed domestically in Kazakhstan either by the producer or by a purchaser. There are special rules for the calculation of tax bases in such cases.

In the case of crude gas that is exported, a flat rate of 10% applies. If crude gas is sold to the domestic Kazakhstan market, the rates are reduced to between 0.5% and 1.5%, depending on the annual production.

[5] Published by The McGraw-Hill Companies Inc.

[6] Published by Argus Media Ltd.

[7] Published by The McGraw-Hill Companies Inc.

[8] Published by Argus Media Ltd.

Signature bonus

The signature bonus is a lump-sum payment paid by a subsurface user for the right to use the subsurface.

For hydrocarbons exploration contracts where reserves have not been approved, the bonus is a fixed amount of 2,800 MCI,[9] which is equivalent to KZT 8,167,600 (approximately US$ 19,000).

For hydrocarbons production contracts and for combined exploration and production contracts where reserves have not been approved, the bonus is a fixed amount of 3,000 MCI, which is equivalent to KZT 8,751,000 (approximately US$ 20,000).

If reserves have been approved, the bonus is calculated by a formula which applies a rate of 0.04% to the approved reserves and 0.01% to the provisionally approved reserves, but not less than 10,000 MCI, which is equivalent to KZT 29,170,000 (approximately US$ 69,000).

CIT

CIT is applied to all companies at the rate of 20% of taxable income. Taxable income is calculated as the difference between aggregate annual income (after certain adjustments) and statutory deductions.

Deductions

All expenses incurred by a taxpayer carrying out activities that are aimed at the receipt of income are deductible for the purpose of determining taxable income. Examples of expenses that are allowed for deduction can be found below (but this list is not exhaustive):

- Interest expense (within limits)
- Contributions to the decommissioning fund. The procedure for making such contributions and the amount are to be established in the subsurface use contract
- Expenditure on geological studies, and exploration and preparatory operations for extraction of mineral resources
- Expenditures on research and development, scientific and technological works

Geological studies, exploration, and preparatory operations for the production of extractable minerals, include the following: appraisal, preparatory work, general and administrative expenses, and costs on the payment of bonuses. These costs, together with expenditure on the purchase of fixed assets and intangible assets (expenditure incurred by a taxpayer while acquiring the right to geological exploration, development, or extraction of mineral resources), form a depreciation group that is separate from fixed assets for tax purposes.

These costs may be deducted applying declining-balance depreciation at a rate not exceeding 25% after production begins following commercial discovery. Similar expenses incurred after the separate depreciation group has been formed (such as expenses incurred after depreciation starts) are included in the group to increase its residual value if, under IFRS, such expenses are capitalized into the value of assets already included in the group.

Depreciation of the pool of such expenses begins when production commences after commercial discovery. In the case of a farm-in, the subsurface user is allowed to capitalize

[9] As of 1 January 2021, the monthly calculation index is established in Law on the Republican Budget for 2021 – 2023 № 379-VI dated 2 December 2020 at KZT 2,917.

the cost of acquiring a subsurface use right. Upon farm-out, the subsurface user is liable for tax on capital gains.

The following are examples of other deductible expenses:

- Expenses incurred under a joint operating agreement are deductible based on information provided by the operator
- Business travel and hospitality expenses (per diems are deducted in full, based on the taxpayer's internal policy, whereas other travel and hospitality expenses are deductible in the amount up to 1% of payroll)
- Net foreign-exchange loss when a foreign-exchange loss exceeds a foreign-exchange gain
- Expenses on social payments to the State Social Insurance Fund
- Insurance premiums, except for insurance premiums paid under accumulative insurance contracts
- Amounts paid as redemption of doubtful payables previously written off as income
- Doubtful receivables not redeemed within three years
- Taxes paid (except for taxes already excluded prior to determining aggregate annual income, income tax paid in Kazakhstan and in any other states, and EPT and ASUT)
- Fines and penalties, except for those payable to the state budget
- Maintenance or current repair expenses
- Capital repairs (within the statutory limits)
- Expenditure actually incurred by a subsurface user with respect to training Kazakhstan personnel and the development of the social sphere of rural areas, within amounts stipulated in subsurface use contracts.

The Tax Code also provides for certain expenses to be deducted directly from taxable income covering up to 4% of taxable income, such as sponsorship aid and charitable contributions (subject to certain conditions).

The depreciation regime for fixed assets is discussed in Section C.

Dividends

Dividends distributed domestically (i.e. by a local subsidiary to a local parent company) are exempt from taxation via CIT adjustments.

Dividends distributed by a Kazakhstani subsurface user which is a legal entity to a non-resident legal entity are subject to withholding tax (WHT) in Kazakhstan as described in Section E below.

Rent tax on exports

The rent tax on exports is paid by legal entities and individuals that export crude oil and crude oil products. The tax base is calculated as the volume of the exported crude oil and crude oil products multiplied by the world price of crude oil. The world price of crude oil is determined as the arithmetic mean of daily quotations for each of the Urals Mediterranean (Urals Med) or Dated Brent (Brent Dtd) brands in the tax period on the basis of information published in Platts Crude Oil Marketwire published by The McGraw-Hill Companies or, if that source does not provide price information for those brands, using the Argus Crude source.

The tax rates applied to exported crude oil and crude oil products vary, as shown in the next table.

Market price	Rate (%)
Up to US$ 20 a barrel inclusive	0
Up to US$ 30 a barrel inclusive	0
Up to US$ 40 a barrel inclusive	0
Up to US$ 50 a barrel inclusive	7
Up to US$ 60 a barrel inclusive	11
Up to US$ 70 a barrel inclusive	14
Up to US$ 80 a barrel inclusive	16
Up to US$ 90 a barrel inclusive	17
Up to US$ 100 a barrel inclusive	19
Up to US$ 110 a barrel inclusive	21
Up to US$ 120 a barrel inclusive	22
Up to US$ 130 a barrel inclusive	23
Up to US$ 140 a barrel inclusive	25
Up to US$ 150 a barrel inclusive	26
Up to US$ 160 a barrel inclusive	27
Up to US$ 170 a barrel inclusive	29
Up to US$ 180 a barrel inclusive	30
Up to US$ 190 a barrel inclusive	32
Up to US$ 200 a barrel and above	32

The tax period for the rent tax on exports is the calendar quarter.

Alternative Subsurface Use Tax (ASUT)

ASUT may be applied by subsurface users as a substitute for MET, EPT and payment for compensation of historical costs (at the discretion of the subsurface user and upon filing an application for use of ASUT).

ASUT may only be applied by subsurface users carrying out hydrocarbons production on the continental shelf or certain deep oilfield deposits.

ASUT is calculated annually. The taxable base is calculated as the difference between aggregate annual income and deductions determined for ASUT purposes (after certain adjustments).

The tax rates applied to the taxable base are shown in the table below.

World oil price (US$/bbl)	Rate (%)
US$50/bbl inclusive	0
US$60/bbl inclusive	6
US$70/bbl inclusive	12
US$80/bbl inclusive	18
US$90/bbl inclusive	24
From US$90/bbl and above	30

The world oil price is determined in the same way as for MET (please see above).

C. Capital allowances

For tax depreciation purposes, fixed assets are split into four groups. Assets are depreciated at the maximum depreciation rates set out in the table below.

Group	Type of fixed assets	Maximum depreciation rate (%)
I	Buildings and structures (except for oil and gas wells and transmission devices)	10
II	Machinery and equipment, except for that used for oil and gas production	25
III	Office machinery and computers	40
IV	Fixed assets not included in other groups, including oil and gas wells, transmission devices, machinery and equipment of oil and gas production	15

Fixed assets, among other items, include:

- Fixed assets, investments in real estate, intangible assets and biological assets recorded in accordance with IFRS and Kazakhstan accounting standards
- Assets with a useful life exceeding one year, manufactured and/or acquired by concessionaries under concession agreements
- Assets with a useful life exceeding one year which are intended for use in activities that are directed at the receipt of income and were received by a fiduciary for fiduciary management.

Some items not considered to be fixed assets include:

- Intangible assets with an indefinite useful life
- Assets commissioned under investment contracts concluded prior to 1 January 2009.

Subsurface users have the right to apply double depreciation rates in the year of commissioning "newly created" fixed assets, provided they will be used in their contract activities for three years.

Expenses actually incurred on the use, repair, maintenance and liquidation of fixed assets are defined as "subsequent costs" and are deductible in the tax period when they are actually incurred, except for expenses that should increase the balance value of assets in the statutory accounting.

D. Investment incentives

Losses

Losses pertaining to subsurface use contracts may be carried forward for up to 10 years. Tax losses may not be carried back.

Tax preferences

Certain subsurface users extracting hydrocarbons on low margin, highly viscous or worked out oilfield deposits may apply for certain MET preferences.

E. Withholding tax

Generally, income of a non-resident derived from Kazakhstani sources is subject to 20% WHT in Kazakhstan, except for the following:

- Dividends, capital gains, interest and royalty – 15%;
- Income from international transportation services – 5%;
- Insurance premiums in accordance with reinsurance risk agreements – 5%;
- Insurance premiums on insurance risk agreements – 15%.

The WHT rate on dividends, interest and royalty may be reduced under the relevant double tax treaty provided that certain conditions are met.

It should be noted that any type of income paid by a Kazakhstani legal entity to a non-resident legal entity registered in tax blacklisted jurisdictions is subject to 20% WHT in Kazakhstan. There is a list adopted by the Kazakhstan Government of countries with a privileged taxation system.

Taxation of dividends

Dividends paid by a Kazakhstani subsurface user that is a legal entity to a non-resident legal entity are subject to WHT at a domestic rate of 15% (or 20% for entities registered in tax blacklisted jurisdictions established by the Kazakhstan Government as countries with a privileged taxation system (tax havens)). However, this WHT rate may be reduced under the relevant double tax treaty provided that the recipient of dividends is the beneficial owner of such dividends, is a fully operating company, and that all other administrative requirements are met. The application of benefits under a double tax treaty is subject to the relevant Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting ("Multilateral Instrument" or "MLI") provisions.

3-year holding period exemption under domestic law

Further, Kazakhstan tax legislation includes a domestic WHT exemption on dividends received by non-residents (except those registered in tax havens) if the following conditions are simultaneously met:

- at the date when the dividends are accrued, the non-resident has held shares/a participation interest (in relation to which the dividends are paid) for more than 3 years;
- within a twelve-month period preceding the first day of the month of the dividends' accrual, a resident legal entity, which is a subsurface user paying dividends, has been carrying out subsequent processing (after primary processing) of at least 50% of the mineral raw materials mined within that period, including coal, at its own production facilities located in the territory of the Republic of Kazakhstan and (or) those owned by a resident legal entity, which is a related party.

Taxation of capital gains

Generally, Kazakhstan source income of non-residents includes amongst other items:

- capital gains generated from the transfer of shares/a participation interest in a Kazakhstani legal entity;
- capital gains generated from the transfer of shares/a participation interest in a foreign legal entity, if 50% or more of the value of its shares/participation interest or its assets derives from Kazakhstan / assets located in Kazakhstan (i.e. the indirect transfer of shares/a participation interest in a Kazakhstan legal entity).

Gains received by a non-resident legal entity from the disposal of shares or participation interest will be subject to Kazakhstan WHT at a rate of 15% (or 20% for non-residents that are registered in tax haven jurisdictions).

Please note that Kazakhstan applies an extra-territorial capital gains tax regime, i.e. if a nonresident sells its shares in a foreign entity that derives more than 50% of its value from Kazakhstan assets then such a disposal of shares is considered income sourced in Kazakhstan and is subject to Kazakhstan WHT at 15% (or 20% for non-residents that are registered in tax haven jurisdictions).

3-year holding period exemption under domestic law

In accordance with Kazakhstan tax legislation, capital gains may be exempt from taxation in Kazakhstan, provided that the following conditions are simultaneously met:

- the seller is not registered in a tax blacklisted jurisdiction
- the legal entity has owned the shares subject to sale for more than 3 years
- the legal entity whose shares are to be sold is not a subsurface user and does not derive 50% or more of its value from a subsurface user in Kazakhstan.

An entity is not recognized as a subsurface user on the sole basis of its right to extract groundwater and (or) common minerals for its own use, and neither is an entity recognized as a subsurface user who within a twelve-month period preceding the first day of the month of the sale of shares or participating interest has been carrying out subsequent processing (after primary processing) of at least 50 percent of the mineral raw materials mined within that period, including coal, at its own production facilities located in the territory of the Republic of Kazakhstan and (or) those owned by a resident legal entity which is a related party.

F. Financing considerations

A 4:1 debt-to-equity limit applies for both Kazakhstan and non-Kazakhstan sourced financing obtained from, or guaranteed by, a related party or obtained from an entity registered in a country with a preferential tax regime. Interest on debt raised to finance construction should be capitalized.

H. Indirect taxes

Import duties

Kazakhstan is a member-state of the Eurasian Economic Union along with Russia, Belarus, Armenia and Kyrgyzstan.

The import of goods to Kazakhstan from EAEU member-states is exempt from customs duties. The import of goods from other countries is subject to customs duties at the rates established by the Common Customs Tariff of the EAEU.

As part of recent amendments to EAEU legislation, Kazakhstan has approved a full list of goods (almost 3,500 items) to which reduced rates of import duty may be applied. Under EAEU regulations, goods included in this list that have been imported under the release for domestic consumption customs procedure at reduced rates have the status of conditionally released goods and cannot be exported to other EAEU member states.

Average market price for crude oil in the previous periods	Rate for crude oil (US$ per ton)	Rate for light oil products (US$ per ton)
Below US$25/bbl	0	0
From US$25/bbl to US$30/bbl	10	3
From US$30/bbl to US$35/bbl	20	6
From US$35/bbl to US$40/bbl	35	10.5
From US$40/bbl to US$45/bbl	40	12
From US$45/bbl to US$50/bbl	45	13.5
From US$50/bbl to US$55/bbl	50	15
From US$55/bbl to US$60/bbl	55	16.5
From US$60/bbl to US$65/bbl	60	18
From US$65/bbl to US$70/bbl	65	19.5
From US$70/bbl to US$75/bbl	70	21
From US$75/bbl to US$80/bbl	75	22.5
From US$80/bbl to US$85/bbl	80	24
From US$85/bbl to US$90/bbl	85	25.5
From US$90/bbl to US$95/bbl	90	27
From US$95/bbl to US$100/bbl	95	28.5
From US$100/bbl to US$105/bbl	100	30
From US$105/bbl to US$115/bbl	115	34.5
From US$115/bbl to US$125/bbl	130	39
From US$125/bbl to US$135/bbl	145	43.5
From US$135/bbl to US$145/bbl	160	48
From US$145/bbl to US$155/bbl	176	52.8
From US$155/bbl to US$165/bbl	191	57.3
From US$165/bbl to US$175/bbl	206	61.8
From US$175/bbl to US$185/bbl	221	66.3
Over US$185/bbl	236	70.8

Export duties

Export duties are established by each member-state of the EAEU separately.

The export duty for crude oil is calculated based on the average market price of crude oil prevailing on the world crude oil markets for the previous period (from the 20th of the month two months before the month of application of export duties to the 20th of the month one month before). The average market price of crude oil is calculated by the authorized body for implementing tax and customs policy. Export duties for crude oil and light oil products are indicated in the table below:

The export of crude oil is not subject to export duties in the following cases:

- Export of crude oil produced by subsurface users under subsurface use contracts that are not PSAs and that envisage exemption from customs duties for the export of crude oil, except for crude oil exported by subsurface users paying royalty;
- Export of crude oil to EAEU member-states or states that have concluded bilateral or multilateral agreements with Kazakhstan envisaging exemption from customs duties for the export of crude oil;

- Export of crude oil by subsurface users who have completed a mandatory tax audit under certain PSAs concluded with the Government of the Republic of Kazakhstan or a competent authority prior to 2009.

Export duty rates for light oil products are calculated monthly based on the export duty rate for crude oil using a special formula. Export duty rates for most heavy oil products are calculated quarterly by the authorized body in the field of regulation of trade activity using a special formula. In case the average market price for crude oil decreases below US$375 per ton based on monthly price monitoring, export duty rates for oil products are established by the authorized body in the field of regulation of trade activity without applying the formula. The export of oil products is not subject to export duties in, among others, the following cases:

- When the average market price for crude oil is below US$187.5 per ton;
- Exports to the EAEU member-states or states that have concluded bilateral or multilateral agreements with Kazakhstan envisaging exemption from customs duties for the export of oil products.

Value added tax (VAT)

A European Union-style VAT applies in Kazakhstan. The VAT rate has been gradually reduced from 20% in the late 1990s to 12% currently.

Crude oil, crude and associated gas sold in the territory of Kazakhstan are subject to 12% VAT. Export sales of crude oil, crude and associated gas are subject to zero-rated VAT.

Under the Tax Code, international transportation services (including the transportation of oil and gas via trunk pipelines) are subject to zero-rated VAT.

Imports of goods and equipment from the EAEU and other countries are subject to 12% import VAT. Special tax administration rules apply to import VAT.

Registration procedures

VAT registration, a process separate from tax registration, is either compulsory or voluntary. Resident legal entities, branches or representative offices of nonresident legal entities and private entrepreneurs must register for VAT if turnover during the calendar year exceeds 30,000 times the MCI. The threshold is approximately US$ 208,000 for 2021. The deadline for VAT registration is within 10 business days after the end of the month in which the turnover threshold is exceeded. Otherwise, it is possible to register as a VAT payer voluntarily before the threshold is reached or immediately upon incorporation.

Electronic VAT invoicing

All VAT payers are obliged to issue electronic VAT invoices starting from 1 January 2019.

Place of supply rule

The applicability of Kazakhstan VAT is determined based on the deemed place of supply. It is important to note that under the place of supply rules, a service may be physically performed outside of Kazakhstan, but deemed to be supplied inside Kazakhstan for VAT purposes. Examples of services taxed in this way include a supply of a service related to immovable property located in Kazakhstan, or a consulting service performed outside of Kazakhstan for a customer inside Kazakhstan. If the place of supply is deemed to be outside of Kazakhstan, the underlying supply is not subject to Kazakhstan VAT. The rules determining the place of supply are generally as follows:

For goods:

- The place where transportation commences, if goods are transported or mailed
- Otherwise, the place where goods are transferred to the purchaser (it is not clear whether this involves a physical transfer or a transfer of rights)

For works and services:

- The place where immovable property is located for works and services directly related to such property
- The place where works and services related to movable property are actually carried out
- The place of business or any other activity of the customer for the following works and services: transfer of rights to use intellectual property, consulting services, audit services, engineering services, design services, marketing services, legal services, accounting services, attorney's services, advertising services, data provision and processing services, rent of movable property (except for rent of motor vehicles), supply of personnel (commonly referred to as "secondment"), communication works and services, etc.
- Otherwise, the place of business or any other activity of the service provider

Sales of goods or services that are merely auxiliary to a principal sale are deemed to take place wherever the principal sale takes place – no definition of auxiliary sales is provided in the tax legislation.

VAT refunds

The following VAT amounts are refundable to a VAT payer from the budget:

- VAT paid to suppliers of goods or services that were used for the purposes of zero-rated turnover (e.g. export);
- The excess amount of reverse charge VAT in case of purchases of work or services from a non-resident;
- VAT paid to suppliers of goods, work and services that were acquired using a grant;
- The amount of cash overpayment of VAT to the state budget.

Virtual warehouse

Created with the aim of systematization of inventory movement and calculation of inventory balances, the virtual warehouse stores information on inventory in taxpayers' warehouses, electronic documents, movement and write-off of inventory from the virtual warehouse.

Electronic accompanying notes

An electronic accompanying note should be issued upon movement, supply and/or shipment of certain goods. The accompanying note should be submitted by taxpayers in the "Virtual Warehouse" module and signed with an electronic digital signature. Starting from 1 January 2020 the production and turnover of biofuel is subject to mandatory issuance of accompanying notes. The issuance of accompanying notes for other goods will be implemented during 2021. The list of goods which are subject to mandatory issuance of accompanying notes is established by the authorities.

Registration fees

Insignificant fixed fees apply.

Other taxes

A number of other taxes, fees and levies exist. Most are economically insignificant. The more important ones are listed below.

Payroll

Based on Kazakhstan legislation, any income paid for work performed in Kazakhstan (regardless if it is paid inside or outside Kazakhstan) is deemed Kazakhstan source income subject to statutory payroll taxation in Kazakhstan by the tax agent (i.e. the Kazakhstan entity, branch or representative office of a foreign entity responsible for the withholding and remittance of income tax).

In order to be compliant with local legislation, host companies must run a so-called "shadow" payroll procedure to process income for work in Kazakhstan. Foreign income is processed for tax purposes only, while the net payment may be made by the home-country employer.

Personal income tax

Income from employment (both tax residents' and tax nonresidents') including all compensation, whether received in cash or in-kind subject to minor exceptions, regardless of the place of payment of such income, is subject to personal income tax at a 10% rate.

Income received in foreign currency is converted to KZT at the exchange rate on the last business day preceding the date of payment.

Social tax

Social tax ("ST") is an additional direct tax imposed on all Kazakhstan employers that is not earmarked for the social benefit of employees.

Employers must calculate ST at a flat rate of 9.5% of gross income, less the obligatory pension fund contributions and employee's obligatory social medical insurance contributions. The minimum monthly tax base for ST per employee is the minimum monthly salary ("MMS"[10]).

ST must be remitted to the state budget on a monthly basis by the 25th day of the month following the tax period. Monthly social insurance contributions are deducted from the monthly social tax liability (see the Social insurance contributions section).

Social insurance contributions

Employers must make social insurance contributions ("SIC"), which are a part of the social tax, at a rate of 3.5% of income paid to (i) Kazakhstan citizens and repatriated ethnic Kazakhs, (ii) foreigners with a residence permit and (iii) individuals who are citizens of country-members of the Eurasian Economic Union and working under employment contracts in Kazakhstan.

For 2021, income received in excess of 7 MMS (KZT 297,500/approximately US$ 700) per month is not subject to SIC. The minimum monthly tax base for obligatory SIC per employee is the MMS.

Employer and Employee Obligatory social medical insurance contributions ("OSMIC")

Employers must make, at their own expense, employer contributions to the Social Medical Insurance Fund on a monthly basis at a rate of 2% of income paid to employees (applicable to Kazakhstan citizens, repatriated ethnic Kazakhs, citizens of the Eurasian Economic Union country-members and foreign citizens holding a Kazakhstan residence permit).

In addition to employer OSMIC, the employer being a tax agent should withhold and remit to the Social Medical Insurance Fund monthly contributions from income of employees (Kazakhstan citizens, repatriated ethnic Kazakhs, citizens of the Eurasian Economic Union country-members and foreign citizens holding a Kazakhstan residence permit) at 2% of such employee's income.

For 2021, income subject to employer and employee OSMIC is capped at 10 MMS (KZT 425,000/approximately US$ 1,000) per month. The minimum monthly tax base for OSMIC per employee is the MMS.

[10] The MMS for 2021 is KZT 42,500.

Obligatory pension fund contributions

Obligatory pension fund contributions (OPFC) at a rate of 10% of the gross salary of employees (Kazakhstan citizens, repatriated ethnic Kazakhs and foreigners with a Kazakhstan residence permit), must be withheld and remitted to the pension fund by the employer on a monthly basis. For 2021, income received in excess of 50 MMS (KZT 2,125,000/ approximately US$ 5,060) per month is not subject to OPFC. OPFC are deductible for PIT, ST and SIC purposes.

Obligatory professional pension contributions

Under the Kazakhstan Law on Pension Coverage, employers must also make at their own expense professional pension fund contributions at a rate of 5% of the gross salary of employees of certain professions in certain sectors, including, among others, mining, oil and gas, pharmacy and consumer goods manufacturing.

According to Kazakhstan legislation all Kazakhstan tax agents paying income to individuals under service agreements should withhold 10% PIT, 10% OPFC and 2% OSMIC calculated from income paid under the service agreement.

Property tax

Property tax is charged at a rate of 1.5%. Basically, this tax applies to immovable property. The applicability of property tax to specific properties of a subsurface user should be additionally researched.

Contract transfers

The Kazakhstan State has a right of first refusal to transfers of subsurface use rights and securities issued in the established securities market linked to subsurface use rights, in respect of oilfields of strategic importance.

Transfer pricing

Kazakhstan's transfer pricing legislation has wide applicability for all businesses. The impact on subsurface users is particularly strong.

The transfer pricing rules apply to all cross-border transactions even if the parties are unrelated. The transfer pricing rules also apply to certain types of domestic transaction if they involve cross-border transactions, e.g. domestic sales of hydrocarbons by subsurface users that are further exported.

The law prescribes the following methods for determining a market price:

- Comparable uncontrolled price method
- Cost plus method
- Resale price method
- Profit split method
- Net margin method.

Except for transactions involving agricultural products, there is no "safe harbor" allowed in terms of deviation from a market price, although the law does in theory recognize that there may be a range of market prices. In determining market prices under the comparable uncontrolled price method, adjustments to prices are allowed in at least some cases, except where one of the parties to a transaction is registered in a tax haven.

There are several compliance requirements that apply to taxpayers, including subsurface users, depending on the type of taxpayer and its revenues:

1. TP monitoring reporting (the deadline is 15 May of the year following the reporting year)
2. Notification on participation in a multinational group (before 1 September of the year following the reporting year)
3. Three-tier transfer pricing reporting, including:
   - Country-by-country reporting (within 12 months following the reporting year or upon request)
   - Master file (within 12 months upon request)
   - Local file (within 12 months following the reporting year)
4. General TP documentation (upon request).

Dinara Tanasheva
Partner, Tax & Law Services Leader
for Kazakhstan and Central Asia
Tel: +7 (727) 258 59 60
Dinara.S.Tanasheva@kz.ey.com

Roman Yurtayev
Associate Partner, Head of the Business
Tax Advisory Services Department
Tel: +7 (727) 258 59 60
Roman.Yurtayev@kz.ey.com

Doniyorbek Zulunov
Partner, Head of the Transaction Tax
Services Department
Tel: +7 (727) 258 59 60
Doniyorbek.Zulunov@kz.ey.com

Anuar Mukanov
Associate Partner, Head of the Transfer
Pricing Services Department
Tel: +7 (727) 258 59 60
Anuar.Mukanov@kz.ey.com

Vladimir Fesenko
Partner, Head of the People
Advisory Services Department
Tel: +7 (727) 258 59 60
Vladimir.Fesenko@kz.ey.com

EY | Building a better working world

EY exists to build a better working world, helping to create long-term value for clients, people and society and build trust in the capital markets.

Enabled by data and technology, diverse EY teams in over 150 countries provide trust through assurance and help clients grow, transform and operate.

Working across assurance, consulting, law, strategy, tax and transactions, EY teams ask better questions to find new answers for the complex issues facing our world today.

EY works together with companies across the CIS and assists them in realizing their business goals. 5,500 professionals work at 19 CIS offices (in Moscow, Ekaterinburg, Kazan, Krasnodar, Novosibirsk, Rostov-on-Don, St. Petersburg, Togliatti, Vladivostok, Almaty, Atyrau, Nur-Sultan, Baku, Bishkek, Kyiv, Minsk, Tashkent, Tbilisi, Yerevan).

ey.com/ru