As we know, the new Law of the RK “On Transfer Pricing” dated 5 July 2008 No. 67-IV (“Law”) has come into force since 1 January 2009.

The Law contains the references to the regulatory legal acts, which includes:

- Rules of cooperation between custom and tax agencies.
- Rules of transactions monitoring.
- List of goods (works, services) subject to monitoring.
- Rules of agreements conclusion.
- List of the official information sources on market prices.
- List of the foreign countries with preferential taxation
- List of the exchange goods.

In this article I would like to provide some comments on each regulatory legal act and possible difficulties to be faced in the course of application thereof.

Law Specification

As we know, the Law specified the date of the ownership transfer to a buyer as the moment of goods sale. In this respect, the Specification explains what a quoted period is and what the sale moment is. **Quoted period** is a period of pricing, during which the average values of maximal and minimal prices for goods (works, services) considering the price range is determined.

**Date of the ownership transfer:**

- **as to oil** – day of the ownership transfer within a quoted period 5 days prior to the ownership transfer and 5 days after thereof; thereat, the day of the ownership transfer shall be a zero day and shall be defined subject to INCOTERMS 2000 delivery terms;
- **as to exchange and other goods (except for oil)** – day of the ownership transfer within a quoted period not early than 15 days prior to the day of the ownership transfer; thereat, the day of the ownership transfer shall be a zero day and shall be defined subject to INCOTERMS 2000 delivery terms;
- **as to international business transactions with participants to be specified by Article 1.5 and Article 11 of the Law** – date of the ownership transfer to a buyer with regard to all goods shall be the date of delivery of the goods thereto in accordance with INCOTERMS 2000 delivery terms;

*In the latter case the date of the ownership transfer irrespective of whether you sell the oil or any other product (exchange one or another) will be one day.*
So, what is the result?

The Specification provides that if a transaction has been concluded with an offshore company or an interrelated party, then a quoted period will be 1 day.

As we know, pursuant to Article 11.15 of the Law interrelated parties shall be the parties, which sell products to each other with deviation from the market price, i.e. with deviation of 0.1%.

Thereat, it will not be difficult for Tax agencies to identify the deviation in any transaction; therefore, your transaction will be considered as a transaction between interrelated parties.

So, it is resulted that in the course of audit they will detect the 0.1% deviation from the market price, classify your transaction as interrelated party transaction and this is the ground for application of the one-day quoted period for you.

With regard to the other cases the following quoted period have been established:

as to products sold under long-term contracts – the moment of the contract conclusion;

as to credits, loans arrangement – the date of conclusion of credit or loan agreements; if the transaction parties amends the basic terms of credit or loan arrangements, the moment of sale after such amendments will be the date of conclusion of agreement for such amendments to the credit or loan agreements.

as to any other works and services – the date of agreement conclusion when the basic terms thereof are applied not longer than a year.

Moreover, the Specification spells out the differential, which is divided into two types of expenses - fixed and variable. In this respect, the variable expenses include such expenses as losses, inspection, port costs, etc., though we understand that actually such expenses are fixed.

- Port costs always appears when transporting by sea;
- Inspection appears in case of any transshipment, i.e. transition from one type of transportation to another;
- Setting aside the losses, which appears every time, i.e. evaporation when transporting, losses when transshipping, etc.

The abovesaid expenses were always fixed and now they are classified as variable ones, i.e. such expenses may or may not occur.

Rules of cooperation of authorized agencies when controlling transfer pricing

Tax and custom agencies together perform audits (inspections) on transfer pricing. Thereat, the audits shall be performed with regard to the following sectors:

- exchange goods approved by the Government of the Republic of Kazakhstan;
- goods (works, services) subject to monitoring approved by the Government of the Republic of Kazakhstan;

With regard to other products the audits will be appointed:

- on the basis of information on application of transfer prices from the state agencies;
- when performing tax and custom audits in accordance with the tax and custom legislation of the Republic of Kazakhstan.

The problem in this case is that any state agency can send a letter to the Tax Committee saying that a tax payer applies transfer pricing not providing any corroboration.
In so doing, will the tax agencies based on the letter study the facts provided therein, perform monitoring of transactions thereunder, require explanations from a tax payer (the letter may contain unconfirmed facts), i.e. perform complete monitoring of transactions?

Most probably they won’t.

Pursuant to the Law such a letter will be a good reason for tax audit on transfer pricing.

**Rules of transactions monitoring**

Transactions monitoring shall be performed through monitoring of prices applied by parties of the transactions by authorized agencies and through tax payers gathering.

Transactions monitoring will apply to those tax payers, which is to be specified in accordance with the Code of the RK “On taxes and other obligatory payments to the budget” (“Tax Code”).

Transactions monitoring shall be submitted to the Tax Committee on or before 15 April of the year following the reporting period (calendar year) in Excel with hard copies.

Within a year each tax payer included into the list of transactions to be monitored must keep records on all export and import transactions.

Such records need to be kept in Excel; thereat, each delivery needs to be included into the table, i.e. how much has been shipped (10 wagons, for instance) or how much is going to be shipped tomorrow, etc.

It is also important that you will have to submit a complete package of documents on transactions to the Tax Committee. Moreover, you will have to attach documents on keeping the business strategy, pricing forecast, business transactions strategy, reports on International Accounting Standards (financial statements), etc.

It is not clear how important it is for transfer pricing, but there is an approach – the more the better.

Having prepared such records, you shall send the results of transactions monitoring to the Tax Committee on or before 15 April of the year following the reporting period. Thereat, you will attach all documents on the differential (discount) thereto.

Differential (discount) is considered when determining the market price in case of timely and founded submission of the information on transactions monitoring, i.e. in case of the failure to submit or incomplete submission of the documents in the course of transactions monitoring, the data will not be considered even if submitted in the course a tax audit.

**List of goods (works, services) subject to transactions monitoring**

There is a list of goods (works and services) subject to transactions monitoring approved in accordance with the Resolution of the Government of the Republic of Kazakhstan dated 12 March 2009, No. 293.

This list includes the basic commodity items to be exported by Kazakhstani companies as well as:

- construction work
- assembly work
- marketing service
- forwarding service
Now, all companies rendering the abovementioned works and services or use them in their entrepreneurial activity will submit the reports thereon to the Tax Committee, i.e. whom they rendered to or whom they purchased from, what price, in what amount, method of transaction pricing, place of the supplier’s registration, etc.

The procedure for submission of the reports is specified in the Rules of transactions monitoring.

Pursuant this list almost all Kazakhstani companies will submit the reporting to the Tax Committee on the annual basis; in case of the failure to submit such companies will be subject to audit. In so doing, the market price will be the minimal when purchasing and maximal when rendering, which will lead to further great additional charges.

**Rules of agreements conclusion**

Now you can conclude an agreement for application of transfer pricing.

The agreement shall be signed between you and the Tax and Custom Committees of the Ministry of Finance of the Republic of Kazakhstan.

The agreement shall be valid during 3 years from the moment of signing thereof.

**Difficulties that may be met when signing an agreement:**

1. In order to sign an agreement you will have to provide the large list of notarized documents. The big problem may be that Tax agencies may not agree with some of the documents, i.e. you provide all available documents, which may be not coordinated with the Tax agencies and that may cause tax audit.
2. Tax agencies consider the documents provided within 60 business days, i.e. on 59th day you may receive a refusal.
3. Tax agencies may send a request to other states in order to obtain the confirmation of the information contained in your documents. In so doing, the request suspends the period for an agreement conclusion until the reply receipt setting aside the longer periods.

In case of violations in fulfillment of the agreement provisions, Tax agencies may cancel thereof unilaterally.

**List of the official information sources on market prices**

Let me introduce the list of export goods (works, services) and information sources, which may be used when determining the market price:

- Oil and oil products – “Platts”, “Reuters”
- Natural and liquefied gas – “Platts”, “Reuters”
- Cotton – “Cotlook Limited”
- Precious metals – “Reuters”, “Metal Bulletin”
- Ferrous and non-ferrous metals – “Platts”, “Reuters”, “Metal Bulletin”, “Megasoft Russia”
- Financial services – “Reuters”, “Bloomberg”

You may find the complete list in the Resolution of the Government of the Republic of Kazakhstan dated 12 March 2009 No. 292.
“Argus Media”, which provided not only information on the world markets but associated expenses related to products delivery to the world markets as well, has been withdrawn from the list.

Now, it is not clear what may be use in order to confirm the variable expenses?

Moreover, the list does not contain the data on information sources, which could confirm such expenses as the buyer’s premium (fee), forwarding expenses as well as expenses occurred when transporting through third countries.

Thereat, Tax agencies require confirmation of such expenses, however, Tax agencies do not specify what information source should be used.

So, the question - “what should be used for confirmation” - is still actual.

There are no information sources only primary documents, however, we understand that buyer will never submit them as these expenses are their profit. Anyway, the buyer will not provide them to you as they are confidential.

Thus, variable expenses will always a disputable issue and this again causes litigation.

List of the foreign countries with preferential taxation

The Resolution of the Government of the Republic of Kazakhstan dated 31 December 2008 No. 1318 approved the list of countries with preferential taxation.

This list contains 63 territories including:
- Swiss Confederation;
- Grand Duchy of Luxembourg;
- People's Republic of China (Macao and Hong Kong in particular);
- Kingdom of the Netherlands (Aruba and Antilles in particular);
- United Arab Emirates (Dubai in particular);
- Republic of Singapore.

In case of transactions with the countries with preferential taxation, the differential (discount) is not considered when determining the market price.

EXAMPLE

You sell the oil under the Odessa FOB terms and the price of the transaction is defined as follows:

\[
\text{BRENT} - \text{discount} = \text{transaction price}
\]

Discount may include such expenses as freight, inspection, fee, etc.

Then, the expenses incurred by the buyer will not be considered when determining the market price, i.e. the market price will be defined as follows:

\[
\text{BRENT} = \text{transaction price}
\]

and such a way applies to all goods (works and services), if the transaction has been concluded with a company registered in the country with preferential taxation.

List of exchange goods

Pursuant to Article 10.2 of the Law on exchange goods taxation items and tax-related items shall not be adjusted, if a transaction price corresponds to the market price considering the price range
indicated in the officially approved information source, unless otherwise specified by this Article (list of exchange goods is to be approved by the Government of the Republic of Kazakhstan).

If you sell exchange goods, then the moment of sale will be the ownership transfer to a buyer.

In case of long-term agreements indicating a long-term price, the moment of goods sale will be the moment of the agreement conclusion. Thereat, in order to apply the moment of the agreement conclusion you have to consider the following terms:

1. Transaction making under the agreement shall be performed within a month from the date of the agreement conclusion.
2. The market price shall be defined as a price published in the officially approved information sources for long-term agreements as of the day before the day of conclusion.

Thus, if there is no information on your goods in the official information sources, then the sold goods will subject to the terms applicable to the exchange goods.

3. A long-term price shall apply during no longer than a year and shall be confirmed by the final contract between transactions parties or a subsequent contract between a trader affiliated with a transaction party that is the resident of the RK and final consumer, which is an independent party. Documents provided upon the request of the state agencies shall be the proof of the contract execution.

In other words, even if there is information in the official sources but final contract between buyer and final consumer is not available (and it cannot be available as it is confidential), then your goods again will be subject to the terms applicable to exchange goods.

It follows that non-exchange goods will be subject to the same terms as exchange goods are; and in order to confirm your price you will have to provide a big package of documents, which are actually not difficult to obtain.