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Newsletter Kazakhstan

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Issue: April – June 2018 · www.roedl.de/kasachstan | www.roedl.kz

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> Recognition of Interest-Free Loan from a Related Party According to IFRS

From **Amir Nurkassymov**, Rödl & Partner Kazakhstan

This article concerns the relevant key questions of recognition of intragroup interest-free loans. It covers the topics related to the initial recognition and the approaches to the measurement of the fair value according to IFRS 13 “Fair value measurement” and IAS 39 “Financial Instruments: Recognition and Measurement”.

It is known that the financial instruments are one of the most important accounting items. In most cases the fair value of a financial instrument in the context of its initial recognition corresponds to its actual value. But in some cases, parent companies provide cash to their subsidiaries on the interest-free basis or at a low interest rate.

The fair value of the financial instruments is determined according to IFRS 13. It is assumed that the transaction with a related party can indicate a difference between the transaction value and the fair value of the asset or liability.

To decide, if the instrument is a loan at an interest rate lower than the market rate, the company should take into account the terms and conditions of this loan, the relevant common practices in this area and the market situation. The interest rates currently used by the company or other market players for the loans with the same remaining term and the same cash flow structure, currency and credit risks fall into the group of factors indicating that the loan is provided at the market rate.

The fair value of a financial liability subject to repayment at request cannot be lower than the amount to pay at request discounted from the first day, on which the company could be obliged to pay this amount. Consequently, the fair value of the liability from an interest-free loan, the repayment of which can be demanded by the creditor at any time (for instance, a loan subject to repayment at request) corresponds to the amount not lower than its nominal value.

If the loan has no determined maturity date and is valid for an indefinite period of time, it is necessary to take into account these assumptions in the process of discounting, when determining the fair value, because a market player acting to their own advantage will not follow the assumption that the loan will be repaid. We suppose that the fair value of the loans without defined maturity dates, which are not subject to repayment at re-

quest, must reflect the assumptions of the market player regarding the terms of the future cash flows.

Regarding the procedure of recognition of the difference between the fair value and the amount of the repayment received or paid, the creditor plays an essential role. If the loan is provided by a shareholder acting particularly as a shareholder, the arising (in the credit) difference (on the part of the loan privileges received) should be generally recognised directly in the equity, because the loan privileges are actually an additional contribution of the shareholder.

The same principles apply to interest-free loans or loans at low rate granted by associate or joint companies, excluding that the discounting effect on the profit or loss for the period will be excluded only to the extent of the investor's share in the associate of joint venture, because in this case the equity method applies.

The loans between the group companies are distinguished by the possibility, that they are granted on the interest-free basis and do not have any due dates. This fact makes the valuation of the loan more complicated, if it is not clear when the loan will be repaid, what is the amount of payments and for what period the loan has been granted. In this case the following factors should be taken into account:

- if the classification of the loan as a liability is correct;
- if there is no approved procedure of repayment specified in the contract or any other agreement;
- if it is possible to calculate when the loan will be repaid.

If the consideration of this factors leads to conclusion, that there is no alternative accounting procedure, this loan should be considered as "subject to repayment at request". This means it must be valued at its nominal value.

Date	Cash flows	Fair value	Discount	Discount amortisation
20-Nov-2017	2.000.000	1.241.518	758.482	-
31-Dec-2017	-	1.254.882	745.118	13.363
31-Dec-2018	-	1.380.370	619.630	125.488
31-Dec-2019	-	1.518.407	481.593	138.037
31-Dec-2020	-	1.670.684	329.316	152.277
31-Dec-2021	-	1.837.752	162.248	167.068
20-Nov-2022	(2.000.000)	-	-	162.248

Table 1: Interest-free repayable loan with the founder

Appendix to the Table 1:

Debt amount: 2.000.000
 Receipt date: 20. Nov.2017
 Interest rate: 0%

Currency: KZT
 Maturity date: 5 years
 Market rate (NB RK): 10%

Example:

Assuming that on November 20, 2017 the company entered into the on interest-free repayable loan contract with the founder to the amount of 2.000.000 Tenge with a term of five years. In this case the loan contract is interest-free and the settlement amount can be determined according to the year average refinance rates pursuant to the data of the National Bank of the Republic of Kazakhstan.

Postings as of November 20, 2017:

- 1) Financial aid provided by the founding shareholder
Debit: Cash – 2.000.000 Tenge
Credit: Loans received – 2.000.000 Tenge

Further the company discounts the interest-free loan at the chosen interest rate, which must correspond to the settlement rate for the credits of regulated banks for the period of the loan or to the refinance rate of the National Bank of the Republic of Kazakhstan (for instance: 10%). In the result of the calculation of discounted cash flows, the fair value of the loan at the moment of procurement of the loan amounted to 1.241.518 Tenge. The difference corresponds to the additional contribution of the shareholder.

- 2) Recognition of the discount in the equity
Debit: Loans received – 758.482 Tenge
Credit: additional paid-in capital – 758.482 Tenge

Postings as of December 31, 2017:

- 3) Discount amortisation for 2017
Debit: Financial expenses – 13.363 Tenge
Credit: Loans received – 13.363 Tenge

Postings as of December 31, 2018:

- 4) Discount amortisation for 2018
Debit: Financial expenses – 125.488 Tenge
Credit: Loans received – 125.488 Tenge

Therefore, taking into account the importance of this issue, the accountants of companies of all legal forms should appropriately recognise and value the financial instruments in accordance with IFRS.

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> Amendment of the Rules of quantitative control of recruitment of foreign employees in the Republic of Kazakhstan

From **Korlan Alikhanova**, Rödl & Partner Kazakhstan

Kazakhstan is a developing constitutional state, which actively operates on the global basis. In the age of globalisation, when people are free to choose where to live, study and work, the migration law of the country they want to live and to work in is of great importance. Kazakhstan takes appropriate legislative measures in order to improve the economic and business welfare. In this regard, it should be noted, that the Government of Kazakhstan takes measures to facilitate the access to employment in Kazakhstan for foreigners.

The Decree of the Government of the Republic of Kazakhstan of December 15, 2016 (“Decree”) determines the scope of persons, who do not need any work permit. According to item 16 of the Annex to the Decree the first heads of branch offices or of representative offices of foreign legal entities do not need any work permit from the local executive authorities.

On April 17, 2018 the Government of the Republic of Kazakhstan adopted amendments to the mentioned Decree concerning persons, who do not need any work permit in Kazakhstan. In particular, according to these amendments, the foreigners do not need to obtain a work permit, if they are appointed as heads of the Kazakhstani legal entities or their deputies and if 100% of the entity’s share capital belong to a foreign company.

Therefore, the foreign citizens employed as directors or deputies in Kazakhstani companies with 100% share capital belonging to a foreign company must obtain only a category C3 working visa for foreign employees. On the grounds of the working visa the foreign employee is entitled to come and stay in Kazakhstan. Family members accompanying the foreign employee must also obtain a working visa, but they are not allowed to work in Kazakhstan.

Despite the termination of the requirement to obtain a work permit for the mentioned category of foreign employees, the non-compliance with the visa requirements and migration legislation is subject to administrative sanctions to be imposed on the foreign employee as well as on the inviting company in Kazakhstan. In this regard we recommend entrusting the visa proceeding to consultants with appropriate experience.

Foreign citizens are generally appointed as heads of legal entities in Kazakhstan completely owned by a foreign company. This follows the intention of the foreign company to have an executive with the required know-how or with a working experience in the Group and certain corporate skills. In this way the company ensures a certain reliability of the executive officer candidate. In most cases, foreign citizens are employed as directors for the period of establishment of the company, i.e. entrance to the market in Kazakhstan, on the first stage of business development. As far as the operative activities develop and the special aspects of the local market and business environment are studied, foreign directors are replaced with Kazakhstani successors.

We suppose such amendments in the legislation have generally positive effect on the development of the labour market, where the competitive ability and the possibility of professional exchange are very important. Furthermore, the local employees get the experience of cooperation with foreign colleagues in managing positions, learn another approach to the management and thus develop the skills improving their competitive ability in the labour market.

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> The Specifics of Applying the Health Care Exemption from Income Tax

From **Ekaterina Prokofyeva**, Rödl & Partner Kazakhstan

All individuals who have incomes (including payroll) subject to income tax and whose tax is withheld at source or who have to pay taxes independently, are payers of tax on incomes of individuals ("income tax") [for the purposes of the Kazakhstani Tax Code].

The Government of the Republic of Kazakhstan adopted the law on the healthcare exemption from Income Tax. The intent of that law is to reduce income tax withholdings at source; the law is underpinned by Article 348 of the Kazakhstani Tax Code. The exemption is meant to cover [a part of] the taxpayer's expenses for medical services (other than cosmetology services) in an amount not to exceed 8 statutory minimum salaries (SMS) for the calendar year concerned; for example, KZT 28.284 (= the 2018 statutory minimum salary, or SMS) times 8 = KZT 226.272. In other words, this tax exemption may not exceed KZT 226.272 for 2018.

To gain a better understanding as to which services and medicines qualify for this tax exemption, please find below the list of qualifying medical services and medicines provided in Article 348 of the Kazakhstani Tax Code:

Medical services

- Preventive health care services, understood to mean the entirety of medical and non-medical services intended either to prevent development or progression of a disease at an early stage or to control complications and/or organ and tissue injuries developed from the disease;
- Diagnostic services, understood to mean the entirety of medical services intended to recognize a disease or to ascertain non-existence thereof;
- Treatment services, understood to mean the entirety of medical services intended to reverse, to suspend and/or to alleviate a disease as well as to prevent progression thereof;
- Medical rehabilitation (aftercare) services, understood to mean the entirety of medical services intended to preserve or to restore in part or in full the disordered and/or lost body functions of an ill or disabled person;
- Palliative care services delivered under the guidance of a medical officer to an incurably ill person in a specialized hospital unit or an independent medical facility (hospice) or as home care during the terminal stage of disease;
- Skin transplantations as result of a suffered injury or burn;
- Dental care services.

Please note that the above list does not include cosmetology services, such as dental bleaching or corrective surgery other than to correct the consequences of a suffered injury or burn.

There is no statutory list of qualifying medicines. However, expenses to buy medicines qualify for the exemption solely where the medicines were purchased from a pharmacy/an apothecary duly registered with health care authorities as a health care business.

Documents entitling to this tax exemption

Employees desirous to make use of this health care exemption from income tax should apply to the employer for this exemption. The application should be accompanied with the following documents required under Article 348 of the Kazakhstani Tax Code:

- Service contract for procurement of paid health care services which shows service price rates (where such contract has been concluded in writing);
- Price list (extract) showing the service prices;
- Document(s) evidencing payment(s) made for health care services.

The required form of the service contract and of the fiscal receipt evidencing payment for medical services

Questions frequently asked in respect of this exemption often concern the required form of the service contract and fiscal receipt evidencing payments made.

Article 35(3) of the Kazakhstani Code: On People's Health and Healthcare System says that paid medical services should be provided under a service contract between the patient and the health care business that is the service provider.

- The service contract for paid medical services shall include at least the following information:
- Medical service type(s) and scope;
- Duration of the contract for provision of those medical services;
- Price lists for medical and non-medical services and payment terms and conditions;
- Rights and obligations of the contracting parties;
- Procedures for amendment, expansion and termination of the contract;
- Responsibility of the contracting parties under the civil law for breach or improper discharge of their contractual obligations.

The documents have to comply with Rules and Terms for Provision of Paid Services in Healthcare Facilities and the Order: On Approval of Primary Medical Document Forms for Healthcare Facilities issued by the Kazakhstani Health Ministry.

The fiscal receipt shall include at least the following information:

- Taxpayer's name;
- Taxpayer's identification number;
- Serial number of the cash register;
- Number under which the cash register is registered with tax authorities;
- Sequential number of the fiscal receipt;
- Day and time of the purchase (of goods, work, services);
- Purchase price (of goods, work, services) and/or lump-sum purchase amount;
- Fiscal identifier;
- Fiscal data processor and details of the fiscal data processor's website enabling verification of the cash register's check voucher for its authenticity – for cash registers with data re-gistration and/or transmission functionality

Deadlines for use of health care exemptions on income tax

Health care exemptions from income tax shall be used in the tax period (calendar month) of the latter of:

- Delivery of the concerned medical services;
- Payment for the concerned medical services.

Example of the payroll computation:

- 1) Employee's monthly salary rate: KZT 200,000

Standard income tax withholding amount:

[KZT 200.000 (salary rate) less KZT 20.000 (mandatory pension contributions, or MPC) less KZT 28.284 (1 statutory minimum salary, or SMS)] times 0.1 (applicable tax rate of 10%) = KZT 15.171,60

Employee's NET salary = KZT 200.000 (salary rate) less KZT 20.000 (MPC) less KZT 15.171,60 (amount withheld as income tax) = KZT 164.828,40

- 2) Employee's monthly salary rate: KZT 200,000

The employee submitted an application and receipts evidencing payment of KZT 50.000 "for medical treatment"

Income tax withholding amount with the health care exemption:

[KZT 200.000 (salary rate) less KZT 20.000 (MPC) less KZT 28.284 (1 SMS) less KZT 50.000 (expenses for medical services)] times 0.1 (applicable tax rate of 10%) = KZT 10.171,60

Employee's NET salary = KZT 200.000 (salary rate) less KZT 20.000 (MPC) less KZT 10.171,60 (amount withheld as income tax) = KZT 169.828,40

Thus, the amount withheld as income tax is lower by KZT 5.000 in Case 2 and consequently the employee's net salary is higher by KZT 5.000 in Case 2 due to the health care exemption.

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April – June 2018

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Castellers de Barcelona



"Each and every person counts" – to the Castellers and to us.

Human towers symbolise in a unique way the Rödl & Partner corporate culture. They personify our philosophy of solidarity, balance, courage and team spirit. They stand for the growth that is based on own resources, the growth which has made Rödl & Partner the company we are today. „Força, Equilibri, Valor i Seny“ (strength, equilibrium, valour and common sense) is the Catalan motto of all Castellers, describing their fundamental values very accurately. It is to our liking and also reflects our mentality. Therefore Rödl & Partner embarked on a collaborative journey with the representatives of this long-standing tradition of human towers – Castellers de Barcelona – in May 2011. The association from Barcelona stands, among many other things, for this intangible cultural heritage.

Imprint:

Newsletter Kazakhstan;
Issue April – June 2018

Publisher:

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