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NEWSLETTER KAZAKHSTAN

SEIZING OPPORTUNITIES

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→ Law

Increase of the authorized capital of the Limited Liability Partnership (LLP)

Korlan Alikhanova
Rödl & Partner Kazakhstan

Limited Liability Partnership (hereinafter referred to as the "Partnership") is the most preferred forms of incorporation for starting business in Kazakhstan.

If necessary, shareholders of the current Partnership may increase the authorized capital by making an appropriate resolution on increasing the authorized capital. As a general rule, resolution on a matter of changing the amount of the authorized capital shall be made by the qualified majority of at least ¾ votes or shareholders of the Partnership[1] present and represented at the meeting. In other words, resolution made by 75 per cent or more votes of the shareholders is required to increase the authorized capital.

A number of methods for increasing the authorized capital are envisaged by the legislation of the Republic of Kazakhstan. At that it is relevant to note that any increase of the authorized capital is possible only after its payment in full.

Thus for example, the authorized capital can be increased by:

- Additional proportional contributions paid by all shareholders of the Partnership;

- Increase of amount of the authorized capital funded from the Partnership's own capital, including from its reserve capital.

In these cases, amounts of the shareholders' shares will not change.

Moreover, the legislation envisages such methods for increasing the authorized capital which imply recalculation of the equity shares:

- Making additional contributions by one or more shareholders when approved by all other shareholders

- Admitting new shareholders to the Partnership.

Resolution on increasing the authorized capital using these two methods (mentioned above) shall be made by common agreement of all shareholders only.

In addition it is relevant to note that the legislation of the Republic of Kazakhstan does not allow increasing the authorized capital by offsetting of claim of the shareholders to the Partnership. Provision of a loan from the shareholder to the partnership may be given as an example, where the shareholder has the right of claim to the partnership for repaying the amount of loan provided. Loan amount due and payable cannot be offset against the payment of the authorized capital.

Contribution to the authorized capital may be made in the form of money, securities, belongings, property rights, including the rights to the results of intellectual activity and other assets (property).

Shareholders' contributions to the authorized capital in kind or in the form of property rights shall be assessed in the monetary form by the decision of the Partnership shareholders. Case when value of the provided property exceeds the amount equivalent to 20,000 (twenty thousand) monthly calculation indexes (approximately 118,000.00 EUR) is an exception. In this case, assessment must be confirmed by an independent expert.

If the authorized capital is formed in money, then the contributions may be paid in any currency: Kazakh Tenge or foreign currency. Non-

[1] Law of the Republic of Kazakhstan "On Limited and Additional Liability Companies", Article 48.2

resident shareholder shall pay an authorized capital in foreign currency by non-cash transfer only by transferring to the bank account of the Partnership itself. Residents are obliged to notify the National Bank of Kazakhstan on the currency transactions related to contributing money and other assets in order to ensure their participation in the authorized capital or as a contribution to its property. Notification mode includes the provision of information on the currency agreement in the prescribed form to the National Bank of Kazakhstan, which means the resolution on increase in the authorized capital. Notification is confirmed seven (7) business days after the date of provision of the relevant information. In this case, resident member of a currency transaction is issued a standard form document (certificate of notification). Amount of contribution received can be credited by the Kazakhstani bank which serves the bank accounts of the Partnership, subject to presentation of the registration certificate of the National Bank of Kazakhstan only.

Increase of the authorized capital also requires notification to the registration authority. Deadline for notifying the authority of Justice is three (3) months upon the date of making Resolution on increase of the authorized capital . In this case, at least a half of amount the authorized capital is increased by must be paid by the date of notification.

Compliance with the requirement of timely notification of the competent authority is important, as in case of its non-compliance, an increase of the authorized capital will be recognized to be invalid.

CONTACT

Korlan Alikhanova
Lawyer
Head of the legal department
T +7 727 3560 655
korlan.alikhanova@roedl.com

→ Accountancy

Major changes in the currency legislation for non-residents of the Republic Kazakhstan

Kurban Aldeshev
Rödl & Partner Kazakhstan

The Law of the Republic of Kazakhstan "On Currency Regulation and Currency Control" (hereinafter referred to as the "RoK Law") will come into force from 1 July 2019.

Primary purpose of the Law is to introduce the gradual changes in the currency legislation due to the entry of the Republic of Kazakhstan to the World Trade Organization.

Major changes introduced to the RoK Law are as follows:

1. Status of non-resident organizations in terms of the currency transactions;

2. Reduction of circulation of the foreign currency;

3. Increase of control over the capital withdrawal from the country (by companies);

4. Regulation of the currency assets exchange procedure;

5. Specification of the list of currency transactions allowed between the residents.

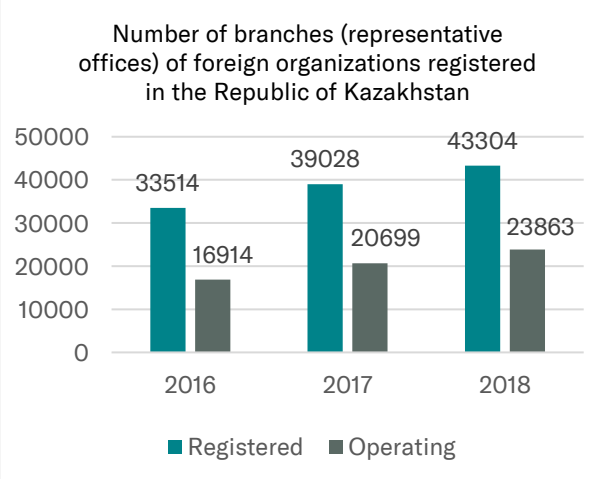
According to the new Currency Legislation, residents of the Republic of Kazakhstan are the companies operating within Kazakhstan. This classification covers the legal entities of the Republic of Kazakhstan, their branches and representative offices, as well as branches and representative offices of the foreign companies within the Republic of Kazakhstan. All foreign companies based outside Kazakhstan will be acknowledged to be non-residents.

Before effectiveness of the new amendments, the branches and representative offices represented by the foreign companies in Kazakhstan have the right to carry out the currency transactions with the residents. From 1 July 2019 the residents of the Republic of Kazakhstan will be obliged to carry out transactions between each other in the national currency of the Republic of Kazakhstan. Branches and representative offices of foreign companies which have entered into an international agreement on behalf of the country with the foreign companies will not be covered by the restrictions on carrying out transactions in the national currency only.

In the meantime, the new Law of the Republic of Kazakhstan does not prohibit the residents in carrying out the currency transactions with non-residents.

Moreover it is relevant to note that transactions under the agreements signed before effectiveness of this Law will not be restricted by the currency control authorities as well.

Kazakhstan government has taken these measures due to the increasing number of branches and representative offices within the Republic of Kazakhstan. Thus, according to the Statistical Agency, the number of branches and representative offices of foreign ownership has increased by more than 4,000 organizations in 2017 only. In return, this inevitably results in increase of the amount of transactions in foreign currency.



According to the National Bank of Kazakhstan, the amount volume of transactions in foreign currency carried out by the branches of foreign organizations with the resident companies was approximately 2.5 billion USD. This situation at the currency market does not coincide with the government interests. Due to this reason, all the calculations will be converted to the national currency.

It is relevant to note that the new Law does not prescribe any restrictions on non-cash purchase and sale of the foreign currency for the purposes of company activities under the signed

agreements, as well as transfer of the national and foreign currency from the bank accounts in Kazakhstan to their accounts in the foreign banks.

The second major change becoming effective from 1 July 2019, is the tightened control over the funds withdrawal. For this reason, the list of currency transactions with signs of funds withdrawal was formed according to the Article 21.2 of the Law of the Republic of Kazakhstan:

a. Financial loan that prescribes provision of funds from non-resident to the resident (except for an authorized bank), unless the terms of the relevant currency agreement provide for the transfer of funds to be received from non-resident to the resident's bank accounts in the authorized banks;

b. Financial loan that prescribes occurrence of the resident's claims (except for an authorized bank) to the non-resident for funds return, unless the terms of the relevant currency agreement provide for the transfer of funds to be received from non-resident to the resident's bank accounts in the authorized banks;

c. Financial loan that prescribes provision of funds from resident to the non-resident (which is not an affiliate) for a period exceeding 720 (seven hundred twenty) days without remuneration payment for using the subject of a financial loan;

d. Export transactions, if the terms of the relevant currency agreement prescribe that the period for fulfilling the obligations to pay for exports by non-resident exceeds 720 (seven hundred twenty) days upon the date of obligations fulfillment by the resident;

e. Import payment transactions, if the terms of the relevant currency agreement prescribe that the period for fulfilling the obligations to return money (advance payment or full prepayment) by non-resident in case of the non-resident's failure to fulfill their import obligations exceeds 720 (seven hundred twenty) days upon the date of obligations fulfillment by the resident.

These transactions will be carried out by the banks, if the sender or the recipient of funds authorizes an authorized bank to communicate information about the payment or funds transfer to the currency control authorities. Transactions which contain the banking secrecy according to the new Law may also be communicated to the tax authorities.

It should be noted that the authorization is not required under the trade or Islamic financing transactions, as well as transactions carried out by non-residents with their branches (representative offices) in the Republic of Kazakhstan, and transactions between branches (representative offices) of the foreign organizations in the Republic of Kazakhstan.

System of the currency agreement registration will be simplified. Currently there are following criteria for registration or notification of the currency transaction: type of transaction, type of the company activities, amount and others. The new Law proposes introduction of the common record registration in terms of amount and subject of the agreement.

Criteria of amount do not change. Part of the criteria is specified below:

- Placement of securities of non-residents at the Kazakhstani market – over 100,000.00 USD;
- Purchase of the residents' securities, residents' units of investment funds by non-residents (except for direct investments) – over 500,000.00 USD;
- Transactions with the derivative financial instruments between residents and non-residents – over 100,000.00 USD;
- Commercial loans related to the export (import) of goods and financial loans provided to the residents by non-residents for a period exceeding 180 (one hundred eighty) days – over 500,000.00 USD;
- Transfers from non-residents to the residents on acquisition of the real estate title – over 500,000.00 USD;
- Transfers from non-residents to the residents on trust management – 500,000.00 USD.

Full list can be found on the official website of the National Bank of Kazakhstan (www.national-bank.kz).

Generally, amendments of the currency legislation cannot be called as highly negative, and aggravating the position of non-residents in Kazakhstan. However, this will definitely make certain adjustments in the relationship between residents and non-residents in terms of signing agreements.

Finally, it is relevant to note that acceleration of signing of the currency agreements with resident partners will let the non-resident branches and representative offices existing or planning to enter the Kazakhstani market next year, keep the terms under such agreements after effectiveness of the Law of the Republic of Kazakhstan.

CONTACT

Kurban Aldeshev
Accountant
T +7 727 3560 655
kurban.aldeshev@roedl.com

→ Audit

IFRS 15 „Revenue from contracts with customers“

Amir Nurkassymov
Rödl & Partner Kazakhstan

The objective of IFRS 15 is to establish the principles that will be applied for determining the nature, amount, timing, and uncertainty of revenue arising from a contract with a customer. This article will focus on the application of the standard using a five-step model and its effects on an entity's accounting.

REASONS FOR THE IMPLEMENTATION OF THE NEW STANDARD

Depending on business circumstances, there is a risk of inaccurate revenue recognition and uncertain picture on the entity's cash flow. The core principle of IFRS 15 is that an entity will recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. A contract asset shall not be recognized as revenue, unlike accounts receivable or actual payments received by the entity for the transfer of goods to the customer. Under IFRS 15, revenue is any income arising in the course of an entity's ordinary activities. The nature of the contract relationship is particularly important for IFRS 15 Revenue from Contracts with Customers. The need for a contract between the parties, in any form, arises due to the emerging obligation to subsequently transfer goods/services and pay for them. Thus, revenue shall be recognized if there is a contract with the agreed terms.

SCOPE

The standard applies to all contracts with customers for the transfer of goods and services except for:

- leases within the scope of IAS 17;
- insurance contracts within the scope of IFRS 4;
- financial instruments and other contractual rights or obligations within the scope of IFRS 9, IFRS 10, IFRS 11, IAS 27, IAS 28.
- non-monetary exchanges between entities in the same line of business to facilitate.

REVENUE RECOGNITION UNDER IFRS 15 USING THE FIVE-STEP MODEL

IFRS 15 applies based on the guidance delivered in a five-step model framework:

1. Identify the contract(s) with a customer;
2. Identify the performance obligations in the contract;
3. Determine the transaction price;
4. Allocate the transaction price to the performance obligations in the contract;
5. Recognize revenue when (or as) the entity satisfies a performance obligation.

1. <u>Identify the contract with the customer</u>

During a business transaction, there is a risk of non-payment by the responsible party. Under IFRS 15, revenue shall be recognized only if it is highly probable that the consideration to which the entity is entitled will be collected. Under the new standard, it is essential for the entity to analyze the contract to determine if it meets the required criteria, as well as to identify risks that may arise during its implementation.

<u>Example 1:</u>
Under the contract, the vendor undertook to supply 200 items of goods (with the price of KZT 1,000 per item). The goods are transferred at some point during a two-month period. Upon receipt of the 100 items agreed, the contract was renewed (modified) by agreement of the parties to increase the quantity of goods by 100 items.

If the additional quantity is sold at a different price, e.g. KZT 900 per item, and this occurs during the term of the main contract, the additional product is separate from the original product, so the revenue under the modified contract is recognized as if it is under a separate contract and shall not affect the revenue recognition under the original contract. Thus, after the obligations under the contract have been fulfilled, the entity will recognize a revenue of 200 × 1,000 = 200,000 under the original contract and 100 × 900 = 90,000 under the modification.

2. Identify the performance obligations in the contract

For the standard to apply, the entity should identify as a performance obligation a good or service (from the goods or services promised to the customer) that is distinct. Initially, it is necessary to assess the promised goods and services in terms of performance obligations in accordance with the terms of the contract using the criteria set forth in IFRS 15. A major factor is whether a good or service or a bundle of goods or services is considered "distinct": If goods or services are distinct, the obligations to transfer them shall be accounted for separately for the purposes of revenue recognition.

Theoretically, a good or a services is distinct, if the customer is able to benefit from the good or service either on its own or together with other resources, and if the good or service is separately identifiable from other goods or services in the contract.

3. Determine the transaction price

The transaction price is the amount to which an entity expects to be entitled in exchange for the transfer of goods and services promised to the customer, excluding amounts received from third parties (e.g. VAT, sales tax).

The transaction price may include variable consideration which can arise, for example, as a result of discounts, performance bonuses, incentives and other similar items. Where a contract contains elements of variable consideration, the entity will estimate the amount of variable consideration to which it will be entitled under the contract. The price will also vary by the value of money over time, if the contract contains a significant financing component. The significant financing component exists, if there is a difference between the promised amount of consideration and the "cash selling price" and if the time between delivery and payment is more than one year.

In order to adjust the consideration, the entity should apply the discount rate which should take into account the credit risk. The discount rate is fixed and will not change, neither in case of changes in interest rates nor in any other case.

Example 2:
The entity sells equipment for 3,000 USD equivalents in case of prepayment. Delivery will be delayed by three years after payment. The passive rate is 6 per cent, considering the credit risk of the seller.
At the moment of payment:
Dt Cash
Ct "Performance Obligation"– 3,000 USD equivalents
During the three years prior to the date of delivery, expenses on interest shall be recognized:
Dt Interest Expenses
Ct "Performance Obligation" 3,000 – 3,000 × 1.06 × 1.06 × 1.06 = 573 USD equivalents (at the time of delivery).
At the moment of transfer of the goods after three years:
Dt "Obligation"
Ct "Revenue" 3,000 + 573 = 3,573 USD equivalents

4. Allocate the transaction price to the performance obligations in the contract

The objective when allocating the transaction price is to ensure the amount allocated to each performance obligation represents the amount of consideration to which an entity expects to be entitled in the exchange.

A good example of a stand-alone selling price of goods or services is the observed price at which the goods or services are purchased by the buyer in a similar situation and conditions. If the stand-alone selling price is not directly observable, it should be estimated by assessing market expectations and projections of future costs or by deducting the sum of observed stand-alone selling prices for other goods or services included in the contract from the total transaction price.

5. Recognize revenue when (or as) the entity satisfies a performance obligation

As a rule, the entity delivers the goods and services promised to the customer over a certain prescribed period. Revenue is recognized as soon as the entity has fulfilled its obligations. The entity must pass the control over the goods or services during the period (and therefore performs the obligation and recognizes revenue over time), if one of the following criteria is met:

- the customer simultaneously receives and consumes all of the benefits provided by the entity as the entity performs;

- the entity's performance creates or enhances an asset (e.g. unfinished production facility) that the customer controls as the asset is created or enhanced;

- the entity's performance does not create an asset with an alternative use to the entity and the entity has an enforceable right to payment for performance completed to date.

In conclusion, it should be pointed out that revenue accounting based on IFRS 15 will change significantly for many organizations. In particular, the new standard will affect companies in the licensing sector and software sales, telecommunications, construction, asset management, etc. Therefore, it will be necessary to develop new assessments, professional approaches and judgments, and perhaps to reorganize the accounting processes.

CONTACT

Amir Nurkassymov
Auditor
General Director of Rödl & Partner
Audit Kazakhstan
T +7 727 3560 655
amir.nurkassymov@roedl.com

→ Company news

Opening of our office in Tashkent

We are pleased to inform you about the opening of our office in Tashkent, Uzbekistan. In doing this Rödl & Partner continues its successful way of internationalization.

With Uzbekistan, Rödl & Partner is developing another key market in Central Asia. Since 2009, the company is already represented in Almaty, Kazakhstan.

Heads of the branch are Dr. Andreas Knaul, responsible for Russia and Central Asia, as well as Michael Quiring, Deputy Head of the offices in Kazakhstan and Uzbekistan.

CONTACTS

Dr. Andreas Knaul, LL.M., d.i.a.p. (E.N.A.)
Attorney at law, Partner
Branch manager in Russia and Central Asia
T +7 495 9335 120
andreas.knaul@roedl.com

Michael Quiring
Attorney at law, Partner
Deputy branch manager in Kazakhstan and Uzbekistan
T +7 727 3560 655
michael.quiring@roedl.com

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Rödl & Partner Kazakhstan
Dostyk ave. 188, BC „Kulan“, 8 Stock
050051 Almaty
T + 7 727 3560 655
www.roedl.com/kazakhstan

Responsible for the content:
Michael Quiring
michael.quiring@roedl.com

Layout:
Diana Tsoy
diana.tsoy@roedl.com