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Foreword

In 2017 Kazakhstan was invited by the OECD to become Adherent to the OECD Declaration on International Investment and Multinational Enterprises. This adherence bears witness to the determination that Kazakhstan holds towards its integration into the world economy and promoting development through responsible business practices.

As an adherent to the Declaration, Kazakhstan commits to providing national treatment to foreign investors and promoting and enabling responsible business conduct. In turn, it benefits from similar assurance from other adherents to treat Kazakh investors abroad fairly and to encourage their multinational enterprises operating in Kazakhstan to contribute to economic, social and environmental progress. In accordance with the OECD Guidelines for Multinational Enterprises, an integral part of the Declaration, Kazakhstan has committed to establish a National Contact Point charged with promoting responsible business principles and practices embodied in the Guidelines, handling related inquiries in the national context and providing a mediation and conciliation platform for resolving practical issues that may arise.

The Investment Policy Review of Kazakhstan *took place under the aegis of the OECD Investment Committee and as part of the OECD-Kazakhstan Country Programme. This publication draws on the report supporting the examination by the Investment Committee of Kazakhstan's application for adherence to the Declaration. The examination of Kazakhstan's investment policies took place in October 2016 at the OECD in Paris in the presence of a delegation from Kazakhstan led by Mr. Yerlan Khairov, Vice-Minister for Investments and Development.*

The Review has been prepared under the supervision of Stephen Thomsen, Head of Investment Policy Reviews, by a team led by Frédéric Wehrlé and comprised of Tihana Bule, John Hauert, Fernando Mistura, Monika Sztajerowska, and Coralie Martin, all from the Investment Division of the OECD Directorate for Financial and Enterprise Affairs, and Narine Nersesyan, then Senior Economist at the OECD Centre for Tax Policy and Administration. It has benefited from discussions in the Investment Committee and comments from the OECD Secretariat, including the Secretariats of the Competition, Corporate Governance, Fiscal Affairs and Trade Committees. The Review has also benefited from inputs provided by the OECD Anti-Corruption Network for Eastern Europe and Central Asia and CleanGovBiz Initiative. The Review is made possible thanks to the financial support from Kazakhstan. The contents are the responsibility of the OECD and do not necessarily reflect the views of the Government of Kazakhstan.

The information in this Review is current as of 1 January 2017.

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Acronyms and abbreviations

ACN	Anti-Corruption Network for Eastern Europe and Central Asia
BIT	Bilateral Investment Treaty
CEOs	Chief executive officers
CIIC	Communication, informatisation and information Committee
CIS	Commonwealth of Independent States
CIT	Corporate Income Tax
CPI	Corruption Perception Index
CSR	Corporate Social Responsibility
DB	Doing Business
EAEU	Eurasian Economic Union
EBRD	European Bank for Reconstruction and Development
EC	Entrepreneurial Code
EITI	Extractive Industries Transparency Initiative
ENT	Economic needs test
ESG	Environmental, social, governance
EU	European Union
FDI	Foreign direct investment
FET	Fair and equitable treatment
FIC	Foreign Investors Council
FTA	Free Trade Agreement
G7	Group of 7
G20	Group of 20
GATS	General Agreement on Trade in Services
GCR	Global Competitiveness Report
GDP	Gross Domestic Product
GFCF	Gross Fixed Capital Formation
GPA	Agreement on Government Procurement
GVCs	Global value chains
ICTs	Intra-corporate transferees
IFC	International Finance Corporation
IGCs	Intergovernmental Commissions
IIA	International investment agreement
ILO	International Labour Organisation
IMF	International Monetary Fund
IPO	Initial Public Offering

IPR	Intellectual Property Rights
ISC	Investor Services Centre
ISO	International Organization for Standardization
ISDS	Investor-state dispute settlement
IT	Information Technology
ITC	International Trade Center
KASE	Kazakhstan Stock Exchange
KREMZK	Committee on Regulation of Natural Monopolies and Protection of Competition
KZT	Tenge Kazakhstani
M&A	Merger and Acquisitions
MFN	Most-Favoured Nation
MID	Ministry for Investments and Development of Kazakhstan
MNEs	Multinational Enterprises
MoU	Memorandum of Understanding
NAP	National Action Plan
NCE	National Chamber of Entrepreneurs
NCP	National Contact Point for the OECD Guidelines for Multinational Enterprises
NT	National treatment
OECD	Organisation for Economic Co-operation and Development
OSS	One-Stop Shop
PPPs	Public Private Partnerships
PPPAC	Public Private Partnerships Advisory Center
RBC	Responsible Business Conduct
RIA	Regulatory Impact Assessment
RK	Republic of Kazakhstan
RUB	Russian Ruble
SEZs	Special Economic Zones
SMEs	Small and Medium-Sized Enterprises
SOEs	State-Owned Enterprises
SPAIID	State Programmes on Accelerated Industrial and Innovative Development
SPE	Special Purpose Entity
SRC	State Revenue Committee
SSEI	Sustainable Stock Exchanges Initiative
TFA	Trade Free Agreement
TNC	Transnational Corporation
UNECE	United Nations Economic Commission for Europe
WBG	World Bank Group
WEF	World Economic Forum
WTO	World Trade Organization

Preface

by

Zhenis Kassymbek, Minister for Investments and Development, Republic of Kazakhstan and Angel Gurría, Secretary-General, OECD

Kazakhstan has made unprecedented economic and social progress since the start of the post-independence reforms in the early 1990s. GDP per capita increased by an average annual rate of 5.2% between 1995 and 2016, making the Kazakh economy the fastest growing of all Central Asian countries. In addition to its expanding oil sector, Kazakhstan's strong performance has been supported by major policy reforms, including continuous efforts to liberalise and simplify investment regulation which has helped spur capital inflows. Kazakhstan has also made important progress addressing poverty, however a significant proportion of the population still remains vulnerable on very low incomes.

Indeed, more remains to be done to fulfil Kazakhstan's ambition of joining the top 30 most advanced economies by 2050. In order to achieve this goal, the government is engaged in ambitious reforms to improve the business environment and further reap the benefits of investment. In particular, Kazakhstan's framework for investment takes on board a number of recommendations that were made in the context of the OECD's first *Investment Policy Review* in 2012. Thus, in 2017, the OECD invited Kazakhstan to adhere to the OECD *Declaration and Decisions on International Investment and Multinational Enterprises* (henceforward the *Declaration*). Adherence signals Kazakhstan's commitment to reform and its willingness to align with international best practices.

This second OECD *Investment Policy Review of Kazakhstan* recognises Kazakhstan's achievements but also provides an independent view of what could be done better. In particular, the government will need to diversify the economy away from over-reliance on natural resources. When related activities are included, the oil and gas sector generates as much as 30% of GDP. Going forward, Kazakhstan would also benefit from increasing domestic

entrepreneurship and strengthening competitiveness. It will also need to prove to investors that the institutional system is transparent and accountable.

The *Review*'s recommendations focus on the need to strengthen policy coherence and reform implementation through solid institutions and stronger co-ordination within government and with the business sector. It also stresses the need to maximise the benefits of investment by reinforcing linkages between foreign and domestic businesses, eliminating administrative barriers, reconsidering incentives policy, promoting responsible business conduct, and implementing clearer strategies for attracting investments that can support economic diversification and sustainable development.

The OECD and Kazakhstan's Ministry for Investments and Development (MID) cooperated closely on this study. While the OECD brought its deep, interdisciplinary expertise, the MID drove the cross-agency process, involving the private sector and civil society and providing critical inputs to the *Review*. The *Review* is an important element of a two-year programme to help Kazakhstan adopt OECD standards and thus provides an anchor for its policy reforms. Through this engagement, the OECD and Kazakhstan will continue to work together to design, develop and deliver better policies for better lives in Kazakhstan.

Zhenis Kassymbek
Minister for Investments and Development,
Republic of Kazakhstan

Angel Gurría
Secretary-General, OECD

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Executive summary

Between 2000 and 2011, supported by a sharp oil price increase beginning in 1999, Kazakhstan's economy grew by an average of 8.4%, making the country one of the world's fastest growing economies over the past decade. With the slump in oil prices, the contraction of the Russian economy and the economic slowdown of China, recent years have nevertheless been challenging for Kazakhstan, with real GDP growth slowing from 6% in 2013 to 1.2 % in 2015, and foreign direct investment (FDI) inflows falling by 52% from 2014 to 2015. With excessive reliance on oil, sluggish growth and the decrease of FDI flows, improving further the framework conditions for foreign investment has become among the authorities' foremost priorities for boosting the diversification of the economy and improving citizens' well-being.

Over the past few years, Kazakhstan has made significant progress in improving its investment regime and business environment. The government has notably lifted foreign equity restrictions in air transport and fixed-line telecommunications, allowing for complete foreign ownership. These reforms have brought Kazakhstan closer to OECD standards. As part of its accession to the World Trade Organization (WTO) in 2015, Kazakhstan has also begun to simplify the procedures for hiring foreigners. Additional changes, expected to be implemented within five years of Kazakhstan's accession to WTO, will support an even more open environment for foreign investors. WTO accession has also led to far-reaching changes in Kazakhstan's trade regime, in particular in services; further reductions of trade barriers are expected in the future to facilitate trading activities.

Kazakhstan has also made important efforts to provide adequate levels of investment protection and effective dispute resolution mechanisms. It has also steadily simplified establishment and licensing procedures over the past years, a progress which has been reflected in the country's improved World Bank Doing Business rankings: at the end of 2016, Kazakhstan ranked 35th out of 190 countries – an improvement of 16 places since 2015. The enactment of a new Public Private Partnership law in 2015 and the upgrading of the concession law seek to propel infrastructural development. Tax reforms are also under way in order to increase revenues, which may result in better tax transparency and revisited investment incentives schemes.

Additional efforts are required, however. To be successful, the ambitious plan to attract more foreign investment must be supplemented by further governance reforms, clearer strategies for attracting FDI, and proving to foreign investors that the institutional system is transparent and accountable. More should also be done to foster domestic entrepreneurship and local skills: despite a number of initiatives to strengthen the important economic role of SMEs, the SME contribution to GDP and the share of population employed in the SME sector remain low when compared with other emerging economies and OECD countries.

Another central determinant of Kazakhstan's capacity to attract FDI is the extent to which the regulations and laws governing economic activity are conducive to competition. State and natural monopolies still apply in some significant sectors such as oil transport via trunk pipelines, transmission of electricity, ports and airports, and railways, sectors which are vital for trade and investment in a country the size of Kazakhstan. In addition, several sectors of the Kazakh economy remain difficult to access in practice for investors, due to the prominence of state-owned enterprises (SOEs), despite an active policy of market liberalisation over the past decades. By some measures, SOEs account for approximately 35% to 40% of Kazakhstan's GDP. Given the significant presence of SOEs in many sectors of the economy that have been opened up to market forces, it is important to ensure that they are, to the greatest possible extent, subject to the same competition and corporate disciplines as private enterprises. The government of Kazakhstan is moving in the direction of adhering to high standards of corporate governance. It is also conducting a large-scale privatisation programme which should decrease the SOEs' share in the economy to 15% by 2020.

The success of Kazakhstan in attracting more investment will also hinge on the authorities' management of one of the main concerns of investors: bribery, favouritism and other forms of unfair treatment of business. The authorities appear committed to cleansing the system of corruption. The real test will however be met only through determined implementation of actions on the ground.

Creating an enabling environment for business to act responsibly and meeting the duty to protect the public interest from potential negative impacts of business activities will also help to retain and attract responsible investors, ensure broader value creation and promote more sustainable development. Recent efforts to raise the quality of investment, notably in the extractive sectors and with regards to environment, are crucial for more inclusive growth. Issues nevertheless remain particularly acute in the areas of human rights and employment and industrial relations. The establishment of Kazakhstan's National Contact Point should be at the centre of the efforts and reforms – whose role is to promote awareness of the OECD Guidelines for Multinational

Enterprises as they relate to ensure that supply chain responsibility – a key issue for a more responsible and inclusive globalisation – becomes a regular way of doing business.

This *Review* describes the most recent reforms. Its purpose is to help the government of Kazakhstan prioritise its actions for improving the framework conditions for investment by providing a broad set of recommendations to make the country an even better place in which to live and invest. The information in this *Review* is current as of 1 January 2017.

Assessment and recommendations

Kazakhstan has enjoyed a long period of stability and prosperity, with one of the world's fastest growing economies over the past decade benefitting from high commodity prices. The past 15 years have been in contrast with the immediate post-independence period when the economy suffered from a sharp economic decline. Extensive reforms following independence, in 1991, started bringing benefits, supported by a sharp oil price increase beginning in 1999. Surging commodity prices supported a strong economic performance in particular between 2000-07, reflected in average annual growth of real GDP of 10.2%. On the demand side, growth had been driven by private consumption and private sector investment, fuelled by strong wage expansion and a credit boom increasingly funded by large scale foreign borrowing of Kazakh banks.

Against the backdrop of mostly external shocks, economic growth has nevertheless decelerated since then. Kazakhstan's real GDP growth slowed from 6% in 2013 to 4.1 % in 2014 and 1 % in 2015,[1] owing to a number of reasons including: reduced global demand for Kazakhstan's main export commodities; the sharp decline in global oil prices since mid-2014; and spill over effects from sanctions imposed on Russia, Kazakhstan's major trade partner (notably the KZT appreciation against the sharply falling RUB caused a loss of competitiveness). Foreign direct investment (FDI) flows in Kazakhstan have fallen, on average, by 15% since 2011, and by 52% from 2014 to 2015 (reaching USD 4 billion or 2.2% of GDP). Progress on poverty reduction largely stalled in 2014 and 2015 and growth was expected to remain low at 0.7% in 2016 and not to be higher than 1.0% in 2017.[2]

The ongoing vulnerability to global commodity prices (especially oil prices) has again unmasked the high risks related to inadequate economic diversification as already noted in a first *Review* of Kazakhstan's investment policy, which was published in the OECD *Investment Policy Review* series in April 2012. In the framework of this *Review*, the OECD recommended *inter alia* easier access to agricultural land and the telecommunication sectors for foreign investors; investment policies related to national security guided by the principles enshrined in the OECD *Guidelines for Recipient Country Investment Policies relating to National Security*; more balanced and transparent local content requirements; corporate governance reforms at state-owned enterprises (SOEs);

increased private participation in infrastructure; better enforcement of intellectual property rights (IPR); better financing support for small and medium enterprises (SMEs); more transparent and predictable trade and tax policy; enhanced fight against corruption; and the development of a coherent government strategy on responsible business conduct.

Over the past few years, the government has been attempting to soften the impact of the slowing economy by attracting foreign investment further, in particular in priority sectors of Kazakhstan's economy. The "100 Concrete Steps, a Modern State for All" program set out by President Nazarbayev recognises economic diversification and growth as one of the country's major priorities and a pre-requisite for sustainable development.[3] The Program, also called "Plan of the Nation", is structured around four major pillars of the reform agenda: i) professionalising public administration; ii) enforcing the rule of law; iii) increasing state transparency and accountability; and iv) fostering economic diversification and growth. The "100 Steps" program, the improvement of physical infrastructure (via the "Nurly Zhol Infrastructure Development" program), and the skills-enhancing agenda – aimed at raising the quality of human capital – are all key pillars of the long-term development strategy *Kazakhstan 2050*, which aims to transform Kazakhstan into a diversified economy driven by the private sector and achieve the country's ambition of joining the top 30 most advanced economies by 2050.

Kazakhstan's investment openness

Since the country's independence in 1991, international investment has been viewed by the authorities as delivering important benefits, ranging from enhanced economic growth to job creation. Over the past decades the country has thus introduced a number of measures to remove restrictions on foreign direct investment. These reforms, coupled with buoyant commodity prices, contributed to the dynamic growth of investment during the first decade of this century. The share of inward FDI flows in total gross fixed capital formation and inward FDI stock in gross domestic product (GDP) increased more than ten- and twentyfold, respectively, since early 1990s (currently, remaining at 59% and 32%, respectively), and remains higher than in many other economies in the region. Still, FDI inflows were unevenly distributed to respond to the needs and aspirations of Kazakhstan's society with a strong concentration of the FDI flows and stock in the extractive sector (Chapter 1).

With sluggish growth and a decrease of FDI flows in recent years, improving further the framework conditions for foreign investment has been among the authorities' foremost priorities for attracting and retaining foreign investors in the country. Foreign investors can participate in most sectors of the economy on an equal footing with domestic investors. The government

notably recently lifted the previous equity restriction in air transport and prohibition of foreign capital above a certain threshold in telecommunications. As a result of this move towards greater openness, Kazakhstan is now getting closer to OECD levels in terms of statutory restrictions according to the FDI Regulatory Restrictiveness Index, although it remains above the OECD average. Additional changes expected to be implemented within five years of Kazakhstan's 2015 accession to the WTO, such as allowing operations of branches of foreign-owned banks, will support an even more open and transparent environment for foreign investors (Chapters 2 and 6).

These important initiatives notwithstanding, there still remains variation in terms of statutory restrictions on FDI in comparison with OECD countries. One restriction relates to the use of agricultural and forestry land, a sector where national sensitivities have been particularly acute. Other restrictions are found in guarding (security) services, mass-media, and fixed-lined telecommunications where Kazakhstan either applies total prohibition of foreign investment (in security services), prohibits foreign investment above a certain limit (in mass-media), or subjects foreign investment to approval above a certain threshold (in telecommunications). They are areas where most OECD countries do not find it necessary to maintain restrictions. Beyond their direct impact on the degree of competition, the key risk is that these restrictions constrain investment. Kazakhstan should restrain from applying these restrictions. Limiting the scope of application of exceptions to National Treatment would also signal greater openness to investment.

Ground-level conditions are also still posing constraints on investment, despite recent steps to eliminate some of them. Conditions include labour market tests for foreign managers and specialists hired in Kazakhstan in the framework of intra-corporate transfer; limitations on the number of foreigners for each category of corporate employees; regulatory quotas for work permits; and preferential treatment of domestic suppliers in the subsoil sector. These requirements are generally aimed at economically empowering citizens or at spurring the development of domestic chains. Notwithstanding their legitimate purposes, they risk constraining the investment attraction potential of Kazakhstan, in particular due to the complexity and fragmentation of regulations (Chapter 2). Alternative measures do exist to promote greater domestic involvement, for example business linkage, skills development programmes and support programmes for SMEs (Chapter 5). The OECD in 2012 already called upon the government to undertake an evaluation of local content policies against alternative options for local private sector development. If some of the requirements are to be maintained, there is scope for rationalising the legislative and regulatory framework and make it more transparent and ensure that they achieve their intended purpose without being unduly burdensome for investors.

The need for transparency also applies to the rules governing private investment in so-called strategic assets or sectors of national interest. Kazakhstan maintains national security grounded screening mechanisms which are not always swift and transparent. Ensuring that the legal framework provides guidance as to what considerations Kazakhstan should take into account in making a determination on national interest grounds would mitigate perceived risks by investors, increase investor confidence, and align the country closer with the recommendations contained in the OECD *Guidelines for Recipient Country Investment Policies relating to National Security* (Chapter 2).

Several sectors also remain difficult to access in practice for foreign investors due to the domination of state-owned enterprises (SOEs) and the prominent position of monopoly sectors in the national economy. By some estimates, the public sector accounted for around 40% of GDP at the end of 2015. To address this issue, in October 2015 the government announced the largest privatisation of SOEs since the country became independent in 1991. In all, 783 SOEs and subsidiaries of national holdings, including 65 of the largest Kazakh state-controlled companies in the oil and gas, transport, and nuclear sectors, are to be sold off between 2016 and 2020. The privatisation plan is aimed at reducing the number of so-called quasi-state entities to 15% by 2021 and at transferring 5% of companies owned by the local governments to the private sector. Other reforms are underway, aimed at encouraging competition and entry and operations of private investors in activities formerly reserved to monopolies. Kazakhstan should nevertheless ensure that privatisation encourages more competition in previously monopolistic sectors instead of merely replacing public with private monopolies (Chapter 2).

Yet, given the still prominent position of monopoly sectors and of SOEs in Kazakhstan's economy, measures contributing to a more level-playing field, together with corporate governance standards, would further enhance the country's attractiveness. Kazakhstan's competition legislation has gone through major reforms recently and, as a result of this, the country has now a competition regime that is in many areas based on sound principles. It is nevertheless still in need of further reforms, including the establishment of an independent competition authority in order to minimize the risk of undue influence as well as – as already recommended in 2011 – of an independent regulator for the telecommunications sector. Intensifying reforms in the areas highlighted in the recent OECD peer review of Kazakhstan's competition policy could help advance the country's competition agenda in this regard. Similarly, even if improvements have been made to the corporate governance frameworks for SOEs, enforcement of rules and regulations remains a challenge. As illustrative of this issue, although audit has become mandatory for all SOEs, it has proved to be so far ineffective (Chapter 2).

Balancing investor protection and the government's power to regulate

The attractiveness of Kazakhstan as an investment destination depends not only on the openness of the economy and restrictions that investors may face. Since the last *Review*, Kazakhstan has continued its efforts to offer both domestic and foreign investors an attractive investment climate by seeking to provide adequate levels of investment protection and effective dispute resolution mechanisms (Chapter 3). At the same time, there is an increasing recognition that investment protection policy involves efforts to balance investor protection and the government's right to regulate.

Kazakhstan's Constitution offers relatively general protection to all persons. Kazakhstan's new Entrepreneurial Code from 2016 gives business entities, and investors specifically, more detailed guarantees on the protection of their rights and property. The Code protects against expropriation and unlawful government conduct in particular. The new Entrepreneurial Code reflects laudable efforts to increase the consistency and transparency of the applicable rules. It also seeks to well-tailor the protection it offers by defining different categories of investment, which qualify for different types and levels of protection. Certain regulatory stability assurances, for example, which can play an important role in the quest for balance between investment protection and the government's right to regulate, are only available to economically important investors. Moreover, the Entrepreneurial Code (as well as legislation applicable to the subsurface sector) seeks to specify in which areas governmental legislative and regulatory action may be stabilised. The concepts and mechanisms introduced by the new Code, or taken over from previous legislation, however, are not always easy to apprehend.

Kazakhstan also offers a wide range of dispute resolution mechanisms to protect investor rights and enforce government obligations. Recent government efforts focused on the functioning of the court system to improve the overall investment climate: the court system has been streamlined, and now offers special court procedures for investors. New initiatives seek to foster capacity of the judges, providing for additional qualification requirements and strengthening performance reviews and training (see Chapter 5). The Astana International Finance Centre is poised to include a special court system, based on the English legal system. Investors may also rely on arbitration or mediation mechanisms. Arbitration and mediation have reportedly only been used sparely by investors, but the Kazakh authorities are seeking to improve their attractiveness, and to thereby reduce the case load of the courts. The protection of intellectual property (IP) rights shows the importance of effective enforcement mechanisms: Kazakhstan has improved the overall legal framework for IP rights – not least in the WTO accession

process – but the enforcement of IP rights continues to be a challenge and constitutes a policy priority. While recent indexes and surveys suggest that overall Kazakhstan is on the right way towards enhancing the quality of its court system, some business representatives and investors continue to voice concerns about the independence of the judiciary.

As part of its efforts to improve the investment climate, Kazakhstan has also signed a number of international investment agreements: These treaties typically protect existing covered investments against expropriation without compensation and against discrimination, guarantee fair and equitable treatment, and give covered investors access to investor-state dispute settlement mechanisms to enforce those provisions. In addition to 47 bilateral investment treaties, 44 of which are currently in force, Kazakhstan has also adhered to a number of multilateral investment treaties. In total, around half of Kazakhstan's investment treaties are concluded with adherents to the OECD *Declaration on International Investment and Multinational Enterprises*. The provisions found in most of Kazakhstan's investment treaties are typically relatively broad, leaving arbitrators a lot of leeway in determining the actual scope of protection they provide. Vague standards that fail to clearly reflect government intent may undermine the right balance between investor protection and the power to regulate.

Properly designed investment treaties can help support Kazakhstan's sustainable and inclusive growth objectives and consolidate domestic priorities, such as promoting and enabling responsible business conduct. Investment treaties can also help ensure that investments are not encouraged by lowering domestic health, safety, labour and environments standards as recommended by the OECD *Guidelines on Multinational Enterprises* (see Chapter 7).

Kazakhstan's tax policy

With the view of attracting foreign investment beyond the extractive sector, Kazakhstan has also been offering generous tax incentives. While the merits of tax investment incentives will depend upon the specific objectives of the incentives, the type and mix of incentives provided and the design of the incentives, there is a danger that the benefits of such incentives are likely to be limited, and could contribute to a harmful 'race to the bottom' among countries competing to attract investors (Chapter 4). This is especially the case where tax investment incentives have been introduced without a comprehensive assessment of their costs and benefits. Despite recent efforts aimed at some rationalisation, the current tax regime remains complex. Kazakhstan applies tax reliefs that vary depending on the type of investment, its location, or activity. Tax and non-tax incentives related to so-called special investment projects, priority investment projects or strategic investment projects also

appear to be discretionary as investors, in order to be granted preferences, must enter into negotiations with the responsible state agency. In general, there has been inadequate analysis to assess the effectiveness of tax incentives.

The recent decline in oil prices has highlighted the risks of excessively relying on tax incentives and the importance of broadening the tax base. While the authorities are working on a new tax code, the current context may be a good opportunity to reform Kazakhstan's tax investment incentives system. Thus, eliminating some incentives, designed and introduced at a time of rising oil prices, could provide a relief to fiscal pressures. Kazakhstan's authorities have recently announced their decision to eliminate wasteful tax incentives. Ensuring better consistency between sustainable growth objectives and the overall investment attraction agenda will be crucial in this context. The OECD has developed a number of tools which allow Adherents to the *Declaration on International Investment and Multinational Enterprises* and other interested countries to assist meeting the recommendations contained in the instrument on *International Investment Incentives and Disincentives*, including the *Checklist for Foreign Direct Investment Incentive Policies*. Enhanced engagement with the OECD Committee on Fiscal Affairs could also provide an opportunity to learn from international experience and strengthen the tax policy regime to support investment.

The quality of the tax administration could also be enhanced as it is central to investors' perception of the stability and certainty of Kazakhstan's tax regime and overall investment climate. Despite recent reforms, Kazakhstan's tax officials continue to be seen by investors as sometimes operating in arbitrary ways. Effective guidance primarily directed at tax officials should be in place to deter inconsistent application of rules, enhance predictability, and eliminate rent-seeking opportunities for officials subject to limited accountability (Chapters 4 and 5). As related to responsible business conduct, tax governance and tax compliance should be treated as important elements of enterprise oversight and broader risk management systems and corporate governance (see Chapter 7).

Investment promotion and facilitation

Well-designed and implemented investment promotion and facilitation policies can help countries attract investment into most productive uses, supporting the objectives of economic diversification and private sector development. In recent years, Kazakhstan has implemented several reforms to reduce red-tape and administrative burdens placed on firms as well as to promote its image as an attractive business destination abroad.

In the area of investment facilitation the focus has been primarily on administrative simplification and a removal of certain licensing requirements.

About 30% of all licenses were removed since 2014, and certain procedures clarified or streamlined. These efforts were recognised by some international organisations. For example, at the end of 2016 the World Bank's annual *Doing Business* index ranked Kazakhstan 35th out of 190 countries for 2017 – an improvement of 16 places since 2016 – and lauded the country's efforts to remove bureaucratic barriers, streamline licensing procedures, and introduce legislation to facilitate and hasten new business formation in the country.

Most recently, under the instruction of the President of the Republic of Kazakhstan, the government established a One-Stop-Shop (OSS) for investors, assisting firms in obtaining necessary information, starting administrative procedures and obtaining permits. It currently has a form a physical facility administered by, and located, at the Investment Committee at the Ministry for Investments and Development with offices elsewhere in the country. Still, during the consultations with stakeholders undertaken in the course of this *Review*, it was established that the OSS is still relatively unknown by the businesses operating in Kazakhstan and embassies of top investing countries in the country. Further work could be undertaken to familiarise the business community with the OSS and obtain feedback. If the implementation of the OSS can truly allow better inter-governmental coordination and translate into reduced time and resources spent by firms in obtaining various licenses and permits, this innovation could facilitate establishment of new and expansion of existing projects in Kazakhstan.

The primary focus of recent investment facilitation reforms on administrative simplification may, nevertheless, fail to address the true source of administrative burdens placed on firms, i.e. the quality, transparency and coherence of the domestic regulatory process. Indeed, in 2012, the OECD *Investment* Policy *Review* highlighted that the predictability, coherence, and quality of regulations and administrative procedures remained problematic in Kazakhstan. The changes to the country's ranking on the World Bank's *Doing Business* indicators do not necessarily reflect such aspects. Businesses consulted in the process of this *Review* highlighted that poor-quality regulations as well as their inconsistent interpretation and arbitrary application continue complicating business decisions and create a breeding ground for corruption (Chapter 5). Tax administration, environmental permits, obtaining visa and work permits for foreign staff as well as satisfying local content requirements by firms appear to be most burdensome areas.

Improving the quality of regulatory processes can help ensure that overly stringent, contradictory or poorly-defined administrative procedures are less common, reducing the scope for arbitrary treatment. While the country implemented several reforms to improve the process of creating new regulations in recent years – notably by introducing the regulatory impact assessment (RIA) as an obligatory element of creating new legal acts – there is

still scope for improving the transparency of the regulatory process, including through broadening and systematising the process of stakeholder consultations and performing advance impact assessment of adequate quality and frequency.

In the area of investment promotion, while the institutional set-up for investment promotion has been reformed, numerous institutions with overlapping functions and mandates are still involved in investment promotion in Kazakhstan. It would be beneficial that their roles and modes of co-operation are more clearly defined. This issue is linked to another lacuna – there is currently no investment promotion strategy in Kazakhstan that would clearly outline the government's objectives and available tools. If accompanied by concrete actions plans for individual agencies and an adequate monitoring framework, such a strategy could help the government ensure that investment promotion activities are well-coordinated and achieve intended results. Finally, as mentioned above, the current system of fiscal incentives for investment in Kazakhstan lacks transparency, and could be reformed to reduce opportunities for corruption and ensure level playing field among firms. Overall, while investment promotion in Kazakhstan benefits from high level of political support, it is still burgeoning and requires clear administrative procedures to achieve results and value for money.

SMEs development

Small and medium sized enterprises (SMEs) policy has become a key component of Kazakhstan's overall economic policy and is at the core of the country's 2050 Strategy. In 2012, the *Investment Policy Review* noted that SMEs faced a lack of access to finance. Since then, the government has been implementing multiyear SME strategies, each of them focusing on subsidized loans to SMEs. In addition, business support centres have been established in the country's rural regions. They provide free business support packages like consultations on how to prepare and file tax reports, how to develop business plans and apply for funding, how to register a new business or how to market a business. They also provide educational support programs, including training courses and seminars aimed at increasing the knowledge and skills of existing and potential entrepreneurs in business management.

However low SME contribution to GDP (about 17.5% at the end of 2014 against almost 60% in countries such as Turkey) and low share of population employed in the SME sector (just over 2.5 million people) show that much more could be done to foster entrepreneurship and SME growth. Two-thirds of SMEs in Kazakhstan are individual entrepreneurs, contributing little to employment and value added as well as to productivity growth. Addressing this issue requires a more coherent and comprehensive approach to SME policy. A well-structured overview of various private sector development

programmes, including those directed at SMEs, is missing and implementation monitoring and impact assessment mechanisms are not systemically employed (Chapter 5).

Trade openness

The attractiveness of a country as location for investment depends not only on statutory FDI restrictions, investor protection, business facilitation and other promotion tools, it also depends on the costs of doing business across borders. Trade policy and the quality of physical infrastructure influence directly the ability of local firms to connect to global markets. The WTO entry in 2015 marked an important step in Kazakhstan's reform process. Negotiations had lasted for nearly twenty years and led to far-reaching changes in Kazakhstan's trade and investment regime, in particular in services. The positive effect of WTO entry on Kazakhstan's GDP has been estimated to amount to about 4% and 10% in the medium and long run, respectively (see Chapter 6).

Opening services sectors to trade and investment due to WTO entry was predicted to have the largest impact on the Kazakh economy (over two thirds of total welfare gains). Indeed, the country implemented several reforms throughout its WTO entry negotiation process and committed to further opening of some sectors upon its entry. For example, the maximum foreign equity limit in fixed-line telecommunications (of 49%) was to be removed by mid-2018, and Kazakhstan already lifted the restriction (see Chapter 2). In financial services, allowing operations of branches of foreign-owned banks, by 2020, will also have a further liberalising effect. Last but not least, WTO-induced reforms to the country's local content policies and rules on hiring foreign staff can also reduce some burdens faced by foreign and domestic-owned firms, albeit subject to transition periods and exceptions (Chapter 6).

Overall, while changes to horizontal or sector-specific restrictions to FDI required by the WTO entry have helped significantly liberalise Kazakhstan's FDI regime over time, in some sensitive areas, identified as restrictive or burdensome in the past *Review*, such as hiring of foreign staff, local content requirements, the impact will be felt only gradually. In addition, the removal of de jure restrictions on FDI will need to be accompanied by further investment facilitation and regulatory reform to ensure that improved market access is not hindered in practice by administrative procedures (Chapter 5).

In addition, the WTO entry may have some impact on the predictability of the country's trade regime. Being simultaneously bound by various WTO rules – on tariff and non-tariff barriers to trade, subsidies, and others aspects – can help reduce the scope for hasty or contradictory policy movements, increasing the stability and coherence of Kazakhstan's trade regime. WTO notification and

due process requirements may also help somewhat increase the transparency of the regulatory process. Committed domestic reform of the process of making draft laws and regulations is, however, necessary to achieve tangible results, including through improved consultations and impact assessment (discussed in Chapter 5). Simultaneously, progress in regulatory co-operation at the level of the Eurasian Economic Union and with other trading partners through deep free trade or economic partnership agreements can help reduce non-tariff barriers faced by Kazakh firms abroad and diminish disparity in regulatory approaches among Kazakh authorities and those of its partners.

Last but not least, a committed trade facilitation reform and investment in infrastructure will be critical to help reduce trade costs faced by all firms in Kazakhstan, including foreign investors. As a landlocked country, Kazakhstan relies on an effective network of railway, road, and air transport links for its non-oil exports. Meanwhile, Kazakhstan scores below the OECD average and regional best practices on most available metrics of efficiency of border procedures. In order to ensure that planned reforms are implemented, a degree of diplomacy at the level of the Eurasian Customs Union will be required but also a better oversight of domestically implemented reforms and allocation of targeted capacity building programmes.

Infrastructure investments

Infrastructure also plays a significant role in the country's future as a major enabler of economic development. Infrastructure and basic services facilitate trade and investment by connecting manufacturers to markets. Infrastructure development is needed in several areas, in particular transport. There are a number of barriers that have constrained private financing of infrastructure in Kazakhstan in the past, including lack of adequate framework for Public-Private-Partnerships (PPPs) and inconsistent enforcement of rules. In 2012, noting the inadequacy of the legal framework as well as high presence of SOEs in significant segments of the infrastructural markets, the OECD recommended that Kazakhstan provide more opportunities for private participation in infrastructure.

Since then, in the context of reduced fiscal capacity due to falling oil prices, Kazakhstan has been increasingly interested in promoting public private partnerships for infrastructure as a tool by which to reduce reliance on public investment, draw in private financing, and share risk. PPPs have been seen as instrumental for improving infrastructure provision by mobilising private investment in infrastructure while improving the efficiency in project delivery and value for money. Thus, in 2015 Kazakhstan enacted a new PPP law, updated its concessions law as well as its PPP agency. These actions should bring clarity to the PPP regime and should help Kazakhstan better

mobilise private investment. The true test will nevertheless come with the capacity of public authorities to manage future infrastructure projects. Delivering projects on time and on budget will require building government capacity at all stages, from project design and approval to execution. For PPPs to succeed, it will also be essential that the integrity framework relating to infrastructure investment is strengthened, including conflict of interest and the public procurement system (see Chapter 5).

Combatting bribery and other forms of unfair treatment of business

The success of Kazakhstan in attracting more investment will hinge on the authorities' management of one of the main concerns of investors: solicitation of bribes, favouritism, and other forms of unfair treatment of business. Although Kazakhstan has made progress in its anti-corruption efforts, bribery remains a persistent problem, for example in the context of public contracts, business licensing, tax audits, customs and land fees. Rent-seeking behaviour that guides the appropriation, control, and distribution of key resources by ruling elites is another area of concerns. Promising reforms are nevertheless underway, aimed at strengthening the rule of law, building effective safeguards against corruption, promoting more open and inclusive dialogue to designing anti-bribery measures, improving the regulatory environment for businesses, and modernizing the government machinery, including the public procurement system. The authorities appear committed to cleansing the system of corruption. New laws have been enacted; the authorities have developed the necessary action plans and programmes. They have also established two business ombudsmen as a means of supporting companies that are faced with explicit or implicit demands for bribes and other forms of unfair treatment and of resolving disputes expeditiously (Chapter 5).

These reforms should in time have a direct influence on the perception of the investment climate. For example, business may have greater confidence in investing in the country if they know that, when solicited to pay bribes, they can take their grievance to the ombudsmen institutions for speedy resolution. The real test will however be met only through determined implementation of actions on the ground every day. Existing legal safeguards have also to be reinforced, notably by expanding and effectively implementing asset declaration systems, and, given the role of the judiciary in providing safeguards against possible misbehaviour by public officials, by enhancing the independence and accountability of the judicial system. Strengthening the independence of the newly-established ombudsmen is essential too. Raising awareness within the private sector about preventive measures such as the new Anti-Corruption Business Charter, and facilitating further public-private dialogue on business integrity standards, tools and instruments through dissemination of best

practices will also be important (Chapters 5 and 7). The OECD Anti-Corruption Network for Eastern Europe and Central Asia, to which Kazakhstan belongs, could help advance the anti-corruption agenda in this regard.

Promoting and ensuring responsible business conduct

Kazakhstan has committed to establish a National Contact Point (NCP) for the OECD *Guidelines on Multinational Enterprises*- which are recommendations on what constitutes responsible business conduct (RBC) in the areas of information disclosure, human rights, employment and industrial relations, environment, bribery and corruption, consumer interests, science and technology, competition, and taxation. At the beginning of 2017, Kazakhstan had planned to establish it in the Investment Committee of the Ministry for Investments and Development (MID). The government was also working on a multi-stakeholder Working Party to assist it in its functioning. The Working Party will act both in an advisory and oversight capacity; it will have decision-making power; and will be multi-stakeholder. In the view of the government, the inclusion of different stakeholders in the Working Group is meant to fight conflicts of interest and ensure that the NCP operates in an impartial manner while maintaining an adequate level of accountability to the government and in accordance with core criteria of visibility, accessibility, transparency and accountability. Additionally, including stakeholders outside of the government is meant to ensure that the NCP retains the confidence of social partners and other stakeholders, and fosters the public profile of the Guidelines as envisioned in the Guidelines. The NCP will be staffed by 5 experts under the Investment Committee, who will act as a Steering Committee and whose range of responsibilities will include arranging Working Party meetings, disseminating information, organising seminars and awareness-raising events, maintaining the NCP website, drafting the NCP annual report, receiving complaints under the specific instance procedures and disseminating them to the Working Party for further processing. In addition to bringing in a multi-stakeholder view into the NCP through the Working Party, a dialogue with stakeholders is planned on a regular basis.

In general, awareness of RBC has increased in Kazakhstan in recent years. Numerous public and private initiatives have been established, with notable efforts to promote RBC by Samruk-Kazyna, the sovereign wealth fund and joint stock company; the National Chamber of Entrepreneurs, Kazakhstan's umbrella business organisation; and several civil society organisations. On a policy level, the new Entrepreneurial Code includes a legal definition of social responsibility and commits the state to creating the conditions and not interfering with business activities in this area, a welcome development in light of previously reported practices that social responsibility projects amounted to a charity tax. Although the government has yet to develop a coherent government strategy on

RBC as recommended by the OECD in 2012, some Ministries have implemented RBC-related initiatives, but they have in general been fragmented and on an *ad hoc* basis. Samruk-Kazyna's 2015 Corporate Governance Code is another notable effort. The Code calls for transparency and accountability, respect for human rights, and environmental protection and envisions the development of action plans on sustainable development, with the *Guidelines* mentioned as a relevant international standard (Chapter 7).

In specific areas covered by the *Guidelines*, corporate governance requirements, including as related to disclosure and reporting, are still evolving. While requirements on non-financial reporting have been partially expanded as recommended by the OECD in 2012, they remain weak in practice. However, some promising initiatives to promote transparency have emerged. The inclusion of a specific chapter on Transparency in the Samruk-Kazyna's Corporate Governance Code is a welcome development. Additionally, Kazakhstan Stock Exchange participates in the Sustainable Stock Exchanges Initiative and Kazakhstan has been declared compliant with the Extractive Industries Transparency Initiative, which is particularly notable due to the importance of the extractives sector.

As related to human rights and employment and industrial relations, while Kazakhstan has ratified most relevant international Conventions, issues with the protection of human and labour rights persist in practice, including also as related to business activities. International organisations, some OECD countries, and human rights defenders have raised serious concerns about the legal framework itself, for example as related to the new criminal codes and trade union laws and their negative effect on fundamental freedoms. While in Kazakhstan's view its legal framework is in line with international standards, the recent protests over land reform and the related arrests, detention and criminal prosecutions imply that some of these concerns might not have been unwarranted. The government has responded by delaying the adoption of the amendment in question by a year. On a policy level, reforms in the *2050 Strategy* are in theory based on protecting and upholding human rights; efforts were made to investigate and prosecute responsible parties for the 2011 Zhanaozen casualties; a new Labour Code entered into force as of January 2016 and in the government's view is fully aligned with OECD and International Labour Organisation (ILO) standards. However, in light of the acute nature of these issues, revisiting some of the provisions that the stakeholders have raised concerns about might be warranted.

The government has made notable efforts over the last decade to modernise environmental legislation and address the legacy of the Soviet period, as reflected in an increase in the position in international rankings on environmental performance. Nevertheless, the economy's reliance on fossil fuels and high energy intensity weigh heavily on the environment, with high

greenhouse gas emissions a notable problem. Kazakhstan is vulnerable to climate change and issues with water shortages and considerable pollution, even if improved compared to a decade ago, persist. In an attempt to address these issues, the *2050 Strategy* integrates environmental considerations in economic objectives. Increasing the quality of institutions charged with environmental protection could be prioritised in order to address the reports of administrative complexity and sometimes discretionary decision-making that impede the correct assessment of the true extent of possible environmental impacts of business activities. Some enterprises have complained about the lack of transparency of environmental regulations, and expressed concerns that fines were imposed in an attempt to exert pressure and obtain additional funds. Strengthening disclosure requirements and rules, including on environmental and climate change matters, would also be beneficial.

As noted earlier in this assessment, bribery remains one of the main constraints for doing business in Kazakhstan, despite efforts made by the government to address the issue. Progress has also been made to scale up protection of consumer rights. Obtaining reliable information on products remains nevertheless a challenge for consumers. Kazakhstan could consider supporting and promoting consumer education and information programmes in order to increase the capacity of civil society to be aware of consumer rights, to monitor government policy, and to promote effective defence of consumer rights. Particular efforts could be made to promote sustainable consumption.

There is also still substantial room for improvement to raise the performance of Kazakhstan's education system and to expand economic opportunities benefiting domestic workers. An inadequately educated workforce has been among the most cited problematic factors for doing business in Kazakhstan, while job quality remains an issue for a large number of workers concentrated in several sectors and regions. In particular, concerns about low wages, non-payment of wages and discrimination have been raised by stakeholders when it comes to foreign investors. Efforts to improve the quality of education, particularly of vocational training, have been introduced through the development of "points of growth" – selected new, world-class educational institutions in the area of secondary education, vocational training and tertiary education. Involving businesses, including foreign ones, in developing and adjusting training and learning opportunities to the market needs would be a worthwhile effort. The government could consider incentivising firms to provide on-the-job training and learning opportunities, as well as providing apprenticeships, traineeships and internships (see also Chapter 5).

Although the legal framework that protects the public interest and underpins RBC has been partially established, more efforts are needed to strengthen it further and ensure implementation and enforcement of the

relevant laws. Kazakhstan's adherence to the *Declaration*, and, in particular, the formal establishment of an NCP under the *Guidelines*, will be an opportunity to consolidate existing efforts and further promote RBC principles and standards, both within the government and with the wider public.

The way forward

Promoting foreign investment, reducing the cost of doing business, creating fair competition rules, fostering private sector development, building more efficient and transparent public administrations, ensuring the rule of law and fighting corruption are high on the agenda of the Kazakh authorities. The present *Review* confirms that, since the previous examination by the OECD of Kazakhstan's investment policies, the country has made significant progress in improving its policy framework. Many of the reforms recently undertaken illustrate willingness on the part of the Kazakhstan authorities to take practical measures to improve the overall business climate and attract more foreign investment.

Investment-related policies in areas such as competition, tax, infrastructure, private sector development as well as policies aimed at combatting bribery and at strengthening the rule of law need nevertheless to be further scaled up to support Kazakhstan's objective to attract foreign investors as part of the country's efforts to diversify the economy away from natural resources. In the case of trade policy, there is also scope to build momentum from the recent WTO entry to engage in further deep-reaching trade reforms, both through committed domestic reforms and further collaboration with the main trading partners.

With regards to RBC, although the legal framework that protects the public interest and underpins RBC has been partially established, more efforts are needed to strengthen it further and ensure implementation and enforcement of the relevant laws. Particular attention is warranted to ensure the protection of human and labour rights. Finally, Kazakhstan's newly established NCP could serve as a valuable vehicle for bringing about policy coherence on a wide range of issues that affect the quality of the investment environment, including, for example, labour relations and corporate governance. A robust NCP that operates in accordance with the criteria set out in the Guidelines, retains the confidence of social partners and other stakeholders, and fosters the public profile of the Guidelines has the potential to shape the quality of incoming investments, contributing to a more stable and predictable investment environment based on a level-playing field.

Overall, it has to be noted that Kazakhstan has undertaken numerous reforms in recent years. In some cases, new laws have just been passed, or are yet forthcoming, and it is too early to assess their impact on Kazakhstan's

policy framework for investment, and confidence of firms to invest in the country. While the reformist momentum of the authorities is laudable, the tendency to pass numerous laws in a short period of time can also add to compliance costs by firms and create uncertainty. There is hence a balance to be struck between reforms and legal and institutional turnover that the government grapples with. More frequent use of *ex ante* and *ex post* assessment tools and regular feedback from stakeholders and coordination among agencies may help amend that.

The main recommendations from this *Review* are presented below while more detailed ones are provided in each chapter.

Box 1. **Principal Policy Recommendations**

Horizontal policies

- Ensure that timely preparation of new rules and regulations does not come at the expense of their consistency and clarity.
- Replace fragmented local content policies for greater domestic involvement with more coherent, strategic reform packages, taking into consideration the interactions between policy areas.
- Consider further strengthening safeguards of judicial independence to ensure that proceedings cannot be influenced by considerations of specific interests or the identity of the natural or legal persons involved.
- Bear in mind that regulatory change imposes costs, as repeated changes can cause uncertainties and compliance costs for business.

Investment policy

National treatment

- Consider further liberalisation in sectors that remain relatively closed to foreign investment and where WTO market access commitments have been limited, such as ownership of land.
- Ensure that administrative procedures, including screening mechanisms, do not limit market access in practice in sectors where market access has recently been deepened, such as telecommunications.

National security-grounded restrictions

- Adopt best practices concerning investment policies taking into account the principles of non-discrimination, proportionality, transparency and accountability enshrined in the OECD *Guidelines for Recipient Country Investment Policies Relating to National Security*, and restrain on the application of exceptions based on essential security interest listed under the National Treatment instrument list of exceptions.

Box 1. **Principal Policy Recommendations** *(cont.)*

Key personnel

- Pursue further efforts aimed at simplifying administrative procedures for hiring key foreign personnel to facilitate access of local firms to talent worldwide. Local content requirements are being reduced but, together with other administrative procedures, still remain a barrier. Administrative capacity of institutions dealing with issuing relevant permits could also be strengthened to reduce delays while retaining appropriate control.

Balancing investment protection and the government's power to regulate

- Focus on establishing a regulatory environment which enhances investor confidence. Government commitments to maintain legislation in the future should be carefully evaluated with regard to the government's future ability to regulate. They should be seen as a useful tool to increase investor confidence until an improved overall legal framework ensures adequate predictability and protection.
- Specify investment treaty language to ensure that treaties accurately reflect government intent. Review existing investment treaties to ensure that improved treaty design is also reflected in Kazakhstan's network of existing treaties.
- Manage liability risks under investment treaties actively. The authorities should seek to ensure that different government agencies and officials are aware of treaty policy and the obligations it entails. Efforts to improve the management of risks could include training programs for government officials and the creation of dispute prevention and management mechanisms.

Tax policy and investment incentives and disincentives

- Increase tax revenue to meet the country's public spending and investment needs by streamlining the tax system and eliminating wasteful tax incentives.
- Review policy rationale for offering different levels of protection and tax incentives to different groups of investors. While in some cases there can be benefit in providing certain extra incentives to attract specific investors, e.g. investors in certain sectors and projects or foreign investors, Kazakhstan should seek to guarantee a sound investment climate for all investors and consider the distorting effect of preferences to efficient investment decisions.
- Establish clear guidelines for tax officials to encourage uniform approach and interpretation of the tax provisions.

Investment promotion and facilitation

- Ensure that business views are taken into account in the design of future investment facilitation reforms.

Box 1. **Principal Policy Recommendations** *(cont.)*

- Ensure that investor community is aware of the one-stop-shop (OSS) for business registration, obtaining licenses and permits and going through other administrative procedures.
- Define a clear investment promotion strategy that would outline the goals and tools of investment promotion strategy in Kazakhstan.
- Clearly define responsibilities of different agencies involved in investment promotion activities in Kazakhstan and agree on modes of co-operation between them to share resources and avoid waste.
- Improve the efficiency of Kaznex Invest operations and reorient its functions towards serving investors, not other government bodies.

Trade policy

- Build on the momentum from the WTO entry to engage in further deep trade reforms.
- Engage in trade negotiations with countries with which trade complementarity is high and no free trade agreement exists.
- Pursue ambitious trade facilitation reform to help reduce trade costs faced by all firms. In particular, advance on streamlining and automating border procedures in collaboration with other Eurasian Economic Union members and internally.
- Strengthen regulatory co-operation with the main trading partners to reduce non-tariff barriers to trade.

Infrastructure development

- Take account of the role of the first pilot PPP project in sending market signals to investor about the adequacy of the new regulatory framework for PPPs.
- Build stronger administrative PPP capacities within the government.
- Strengthen integrity frameworks relating to infrastructure investment and the procurement system, including conflict of interest

Competition policy

- Given that the economy is still characterized by the prevalence of a few powerful undertakings as well as monopolistic sectors, keep strengthening the competition law regime, notably in the areas highlighted in the OECD Competition Committee's recent peer review of Kazakhstan, such as improving the independent action of the new competition authority, and ensure that privatisation encourages more competition in previously monopolistic sectors instead of merely replacing public with private monopolies.

Box 1. **Principal Policy Recommendations** *(cont.)*

Corporate governance

- Given that state-owned enterprises (SOEs) are still present in many sectors of the economy, strengthen measures contributing to a level playing-field, including by supporting the enforcement of corporate governance frameworks for SOEs. The OECD *Guidelines on Corporate Governance of State-Owned Enterprises* advise countries on how to manage more effectively their responsibilities as company owners, thus helping to make state-owned enterprises more competitive, efficient and transparent.

Public governance

- Implement determinately anti-bribery and integrity measures, notably in the areas highlighted by the third round monitoring report on Kazakhstan under the Istanbul Anti-Corruption Action Plan and the Integrity Scan of Kazakhstan undertaken under the auspices of the OECD's CleanGovBiz Initiative.
- Pursue on-going efforts aimed at fighting bribery in civil service and promoting public sector integrity, notably through the development of efficient systems that proscribe conflicts of interests. The OECD *Recommendation on Guidelines for Managing Conflict of Interest in the Public Service* advises countries on how to avoid and manage more effectively conflicts of interest.
- Adopt clear and robust implementing rules to articulate the new public procurement law's vision, especially in terms of transparency and accountability, oversight, and fair and equitable treatment for potential suppliers, and reduce the exceptions that limit the application of the law to the greatest extent possible. The 2015 OECD *Recommendation on Public Procurement* advises countries on how to establish a well-functioning public procurement system.
- Take further action, as appropriate in co-operation with business organizations and other civil society stakeholders, to advise and assist companies throughout Kazakhstan in their efforts to prevent bribery through, for example, the development of seminars, guidelines and other forms of guidance.

Responsible business conduct

- Develop a *National Action Plan on Responsible Business Conduct (RBC)*, in collaboration with stakeholders and in line with international good practices. Clearly communicate expectations on RBC, provide guidance on accepted practices, and promote policy coherence and alignment on RBC. Support awareness raising events.

Box 1. **Principal Policy Recommendations** *(cont.)*

- Consider strengthening disclosure requirements for non-financial information in line with international best practice. Ensure, as a matter of policy coherence, that any corporate governance reforms adequately address, describe and reflect the extent of corporate responsibilities related to environmental and social matters.
- Ensure that the legal framework and national system of protection of human and labour rights is aligned with international standards. Make a particular effort to promote the good offices envisioned as part of the mandate of the NCP for the Guidelines as one of the available state-based non-judicial mechanisms for resolving issues related to human rights and employment and labour relations.
- Include RBC expectations in FDI attraction efforts and include RBC criteria in efforts to promote linkages between MNEs and domestic industries, for example, by making RBC one element of supplier databases and matchmaking events. Include RBC principles and standards in industry-specific training programmes for local firms and support training and awareness-raising with business leaders on RBC.
- Involve the private sector in human resource development policies and encourage internal and external training by employers. Communicate to enterprises that contributing to human capital formation (in particular by creating employment opportunities and facilitating training opportunities for employees) is a pillar of RBC – and recognise those that do it.
- Increase the quality of institutions charged with environmental protection and promote compliance with internationally recognised standards as a competitive opportunity that could open up opportunities for international investment and trade.
- Consider introducing initiatives that promote consumer education and information programmes in order to increase the capacity of the civil society to be aware of consumer rights, to monitor government policy, and to promote effective protection of consumer rights. Particular efforts could be made to promote sustainable consumption.

Notes

1. National sources; the World Bank, Country data: Kazakhstan; and the Asian Development Bank website, Kazakhstan: Economy.
2. Asian Development Bank website, Kazakhstan: Economy.
3. English version available on the Kazakh embassy to the United Kingdom website: *www.kazembassy.org.uk/en/pages/page/82* (accessed on 11 July 2016).

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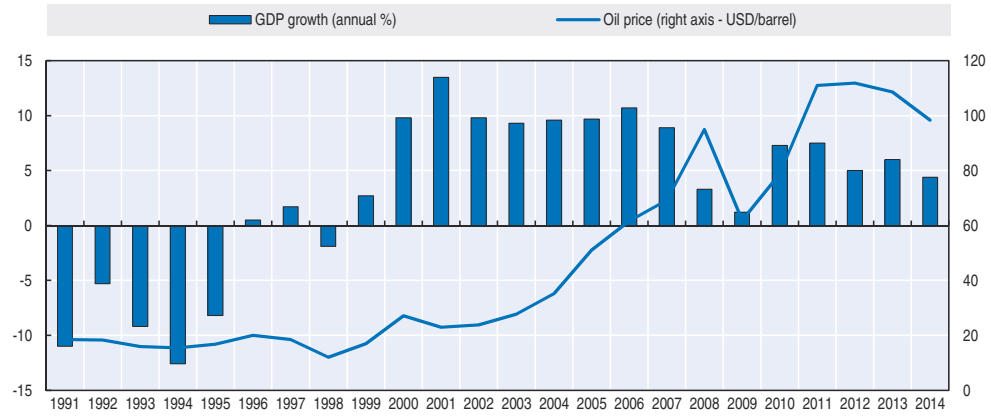
Chapter 1

Foreign direct investment performance and Kazakhstan's economic development

In the light of the current global economic slowdown and stagnating commodity prices, attracting foreign direct investment (FDI) has proven increasingly difficult in Kazakhstan. FDI inflows have declined, on average, by 15% since 2011, and 52% in 2015 (reaching USD 4 billion in 2015). This marks a significant decrease compared to the average of USD 10 billion in annual FDI inflows over the past decade. Still, being a small and remote economy, Kazakhstan has performed well in overall FDI attraction relative to the region, with the share of its inward FDI stock to GDP (of USD 119.8 billion or 55%) being higher than in most neighbouring countries. The principal challenge remains to attract investment into sectors and activities other than natural resource extraction, which accounts for more than 70% of total FDI stock, as well as retain investors already present in the economy.

Ever since its independence Kazakhstan has undertaken a series of reforms aiming at opening of its economy and modernising its productive structure. As captured in the early OECD *Investment Guide to* Kazakhstan (OECD, 1998), the country underwent a series of privatizations, introduced significant legal changes to its regulatory regime, and stabilized its macroeconomic situation throughout the 1990s. After a period of adjustment and economic contraction in the 1990s, the country, aided by buoyant oil prices, stable political environment and continuous reform, experienced a strong economic growth throughout 2000s, the immediate aftermath of the global financial crisis notwithstanding (Figure 1.1).

Figure 1.1. **Annual GDP growth in Kazakhstan and world oil prices, 1991-2014**



Source: International Energy Agency; World Bank's World Development Indicators.

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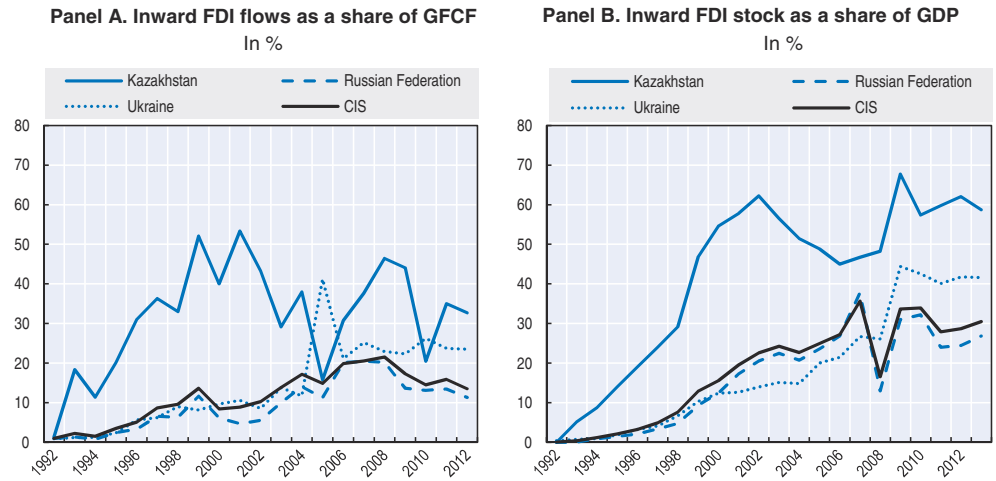
The role of the foreign direct investment (FDI) in the economy has also increased over time (Figure 1.2). The share of inward FDI flows in total gross fixed capital formation (GFCF) and inward FDI stock in gross domestic product (GDP) increased more than ten- and twentyfold, respectively, since early 1990s (currently, remaining at 59% and 32%, respectively). These shares remain higher than in many other economies in the region, even though this partially reflects the small size of Kazakhstan's economy. As testified by the *Investment Policy Review* of Kazakhstan (OECD, 2012), the country has also undertaken a series of important reforms aiming to improve its investment climate, and has

Figure 1.2. **Inward FDI stock as a share of GDP and inward FDI flows gross fixed capital formation (GFCF), 1992-2012**



Source: World Development Indicators and UNCTAD.

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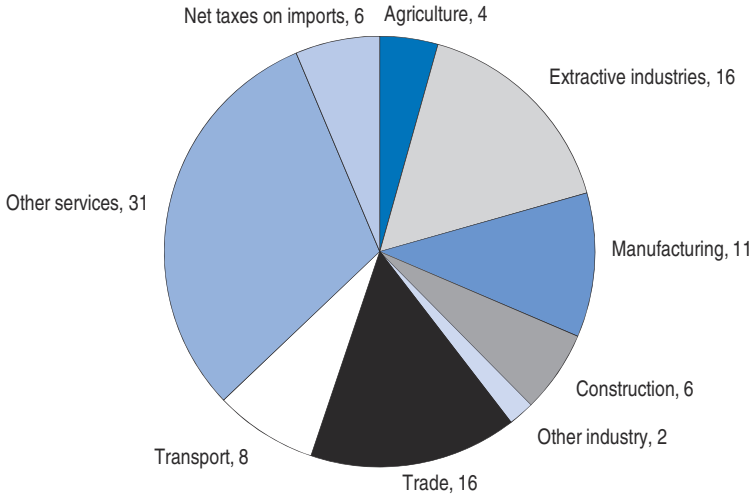
successfully concluded its accession to the World Trade Organisation (WTO), described in more detail in Chapter 6.

Still, given a current slowdown in the global oil prices and a sharp decrease in household spending following strong depreciation of the tenge (KZT), the government has been under increasing pressure to undertake further reforms that help boost growth and diversify its economy, including through stronger attraction of FDI. The oil and gas sector is estimated to account for around 16% of value-added, 30% of GDP, almost a third of budget revenues and two-thirds of exports (OECD, 2016a: 87) (Figures 1.3-1.4).[1] The stability of these metrics over time indicates that, despite economic diversification being the government's announced policy priority, Kazakhstan has struggled to significantly alter its economic base and facilitate the growth of non-traditional sectors. The number of export products and markets in Kazakhstan had not changed much since early 2000s, and remains much lower than in other Commonwealth of Independent States (CIS) countries (Figure 1.A1.1 in Annex 1.A1). As will be explained in Chapters 5 and 6, remaining business climate issues, relative remoteness and limited connectivity with foreign markets, weak competition in certain sectors as well as lack of effective FDI attraction policy may be among the contributing factors.

This chapter presents the recent trends in FDI in Kazakhstan, including dominant sources and sectors for investment to provide an overview of the current role of FDI in the Kazakh economy.

Figure 1.3. **Kazakhstan's GDP by sector, average 2012-14**

In %

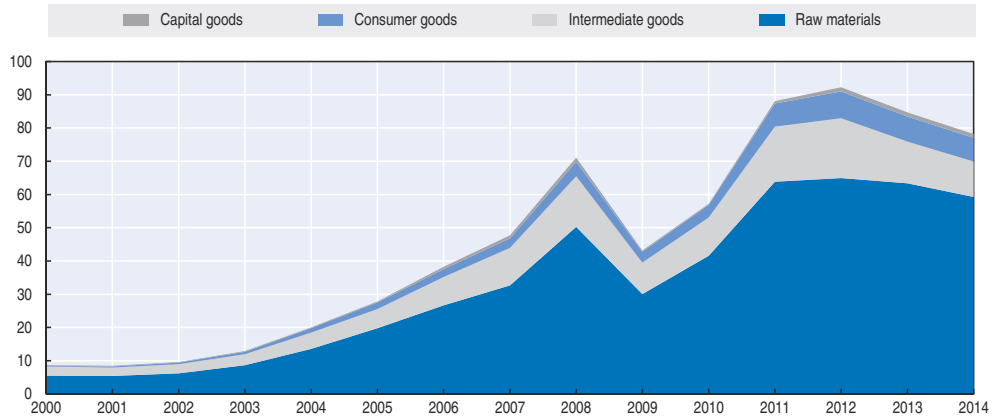


Source: Committee on Statistics, *www.stat.gov.kz*.

StatLink http://dx.doi.org/10.1787/888933452657

Figure 1.4. **Kazakhstan's exports by type, 2000-14**

In billion USD



Source: UN COMTRADE database.

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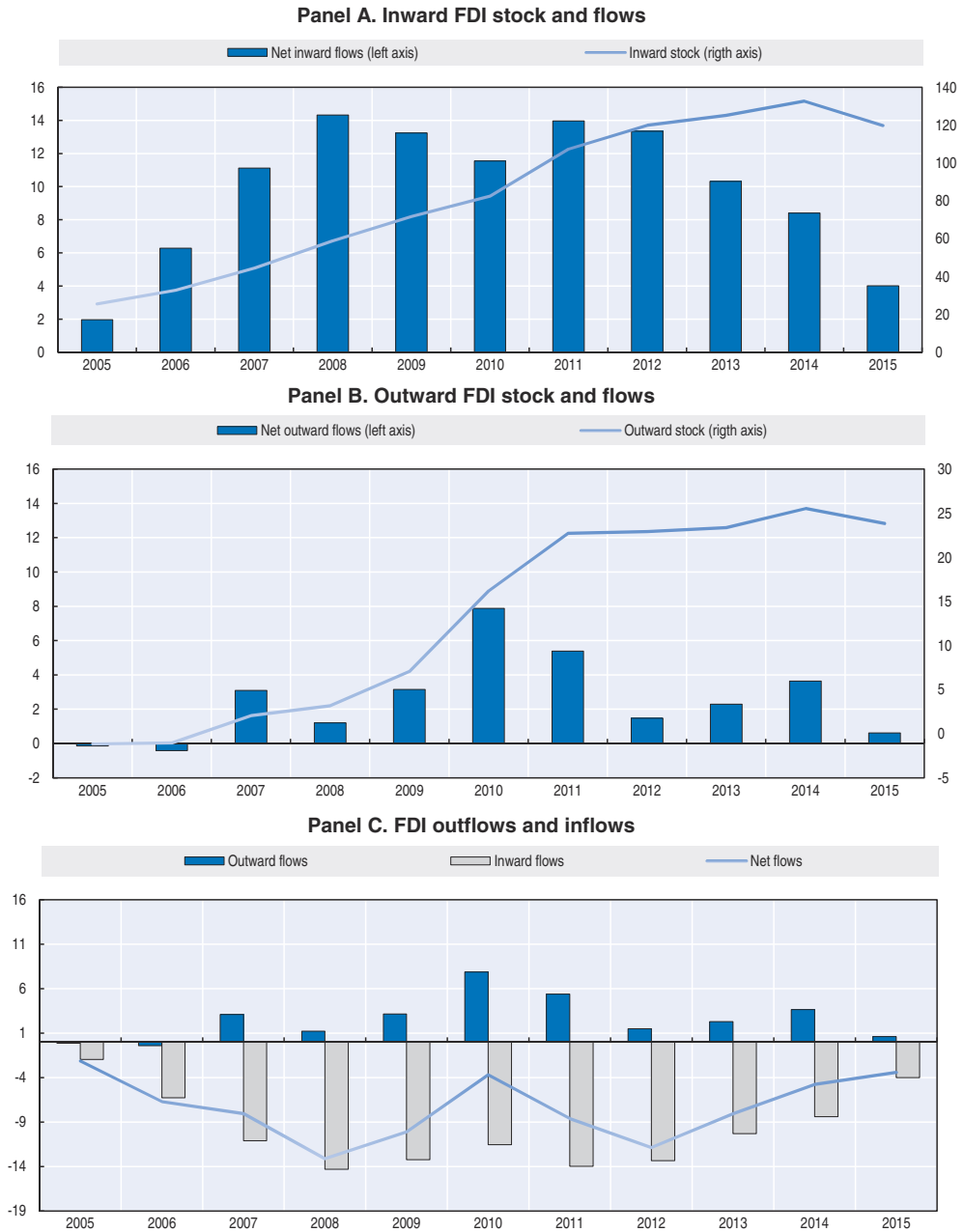
Recent FDI trends

Over the past ten years, FDI inflows have shown a strong cyclicality, reaching peaks in 2008 (of USD 14.3 billion) and 2011-12 (USD 14 billion) (Figure 1.5). After a fall in 2010, FDI has recuperated in 2011-12. Since then, however, FDI inflows in Kazakhstan have fallen sharply, primarily due to the

Figure 1.5. **Inward FDI stock and flows in Kazakhstan, 2005-15**



Note: National Bank of Kazakhstan publishes FDI statistics according to the directional principle with a breakdown to countries and types of economic activities of the residents at *http://nationalbank.kz*.
Source: National Bank of Kazakhstan.

StatLink http://dx.doi.org/10.1787/888933452673

reduced profitability of the domestic oil sector at lower oil prices but also reduced liquidity of firms in other sectors in the aftermath of the crisis. For example, in banking there have been departures of several large global players (see Box 1.1). Meanwhile, the outward FDI flows have remaining relatively flat, averaging USD 2.6 billion per year over the period 2005-15. The inward FDI stock in Kazakhstan has reached USD 119.8 billion (55% of GDP) and outward FDI stock USD 23.9 billion in 2015 (about one fifth of the inward stock or 11% of GDP). Kazakhstan is hence sustaining a net negative FDI position with annual FDI inflows outweighing outflows over the past ten years. The gap has narrowed in recent years with a relatively sharper decrease in FDI inflows than outflows in 2012-15.

Box 1.1. **Foreign divestments in the banking sector in Kazakhstan**

Several global banks have divested their operations in Kazakhstan, partially or fully, in recent years (Table 1.1). Among the more notably ones was the exit from the country of UniCredit in 2013, HSBC in 2014, and RBS in 2015. In all cases, the assets were bought by Kazakh investors (see below). Foreign firms remain to be present in the sector though, with 16 out of all 35 banks having some foreign participation in 2015, including 13 subsidiary banks (see below).

M&A divestures in the commercial banking sector in Kazakhstan, 2005-15

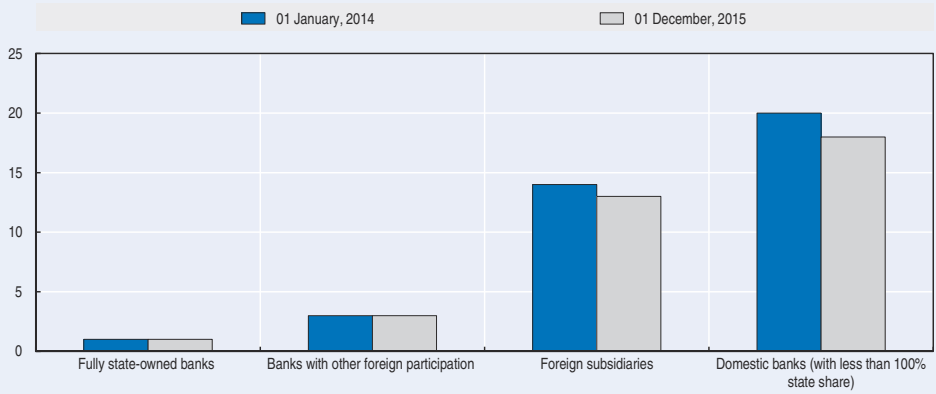
Completion date	Acquiror nationality	Acquiror	Target	Divestor nationality	Divestor	Deal value (min USD)
24-Aug-06	Kazakhstan	QVT Financial LP	Bank TuranAlem OAO (7.7%)	Austria	Raiffeisen Zentralbank Oesterreich AG - RZB	174.8
31-Oct-05	Kazakhstan	Kazkommertsbank OAO	ABN AMRO Asset Management (Kazakhstan)	Netherlands	ABN AMRO Holding NV	-
13-Sep-10	UK	HSBC Holdings plc	RBS Group plc (Retail business, Kazakhstan)	UK	RBS Group plc	52
21-Feb-11	Kazakhstan	Eurasian Bank AO	ProstoKredit MKO	France	Société Générale	-
2-May-13	Kazakhstan	KazNitrogenGaz TOO-KNG	ATF Bank OAO (99.75%)	Italy	UniCredit SpA	470.3
2-Dec-14	Kazakhstan	AlmexHolding Group AO	HSBC Bank Kazakhstan	UK	HSBC Holdings plc	176
31-Mar-15	Kazakhstan	Capital Bank Kazakhstan AO	RBS Group plc (RBS's business in Kazakhstan)	UK	RBS Group plc	-
31-Dec-15	Kazakhstan	Eurasian Bank AO	BankPozitivKazakhstan JSC	Israel	Bank Hapoalim BM	26

The reasons for the divestures of the foreign firms in the sector have been diverse but according to the official announcements appear to be driven by the long-term MNE strategies of focusing on the core markets of their operations and divesting peripheral assets. For example, the UniCredit's decision to close its operations in the country appears to be an outcome of strategic considerations embodied in its five-year plan which include

Box 1.1. **Foreign divestments in the banking sector in Kazakhstan** *(cont.)*

a greater focus on core markets in Eastern Europe, notably Poland. Already in 2011, the group announced that it would be willing to sell Kazakh JSC ATFBank at an appropriate price, and completed the deal with a Kazakh investor, KazNitrogenGaz LLP, in March 2013. UniCredit's Bank Austria, bought ATF (the fifth-largest Kazakh lender) for USD 2.1 billion in 2007. Similarly, the withdrawal of RBS appears to have to have been outlined in its strategic orientations at the MNE headquarter level.

Number of banks in Kazakhstan according to ownership status, 2014-15



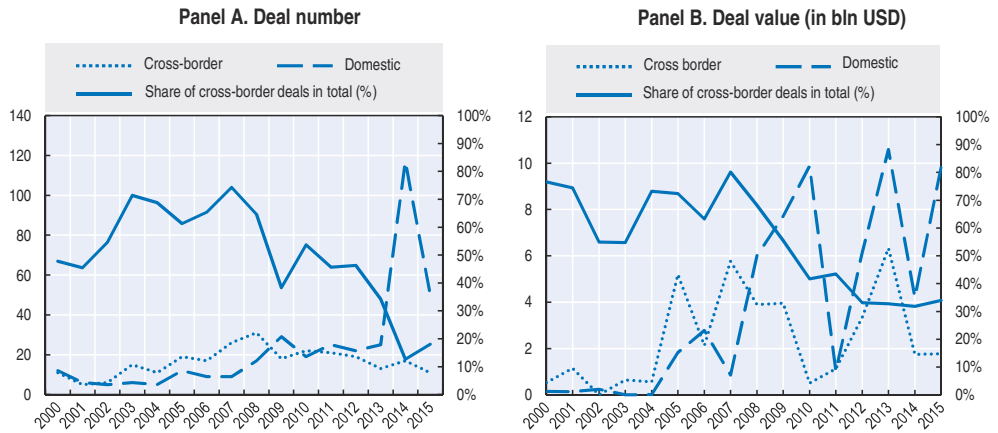
Source: National Bank of Kazakhstan.

In order to ensure that these and other divestments are not caused by weaknesses of business climate and to help retain investments, the government should consider engaging in dialogue with investors that either already divested or announced future divestments on the underlying causes.

Source: UniCredit, Bloomberg, Reuters, National Bank of Kazakhstan, Dealogic.

The trend in declining FDI flows in recent years has been reflected both the declining shares of cross-border mergers and acquisitions (M&A) activity in Kazakhstan, whereby domestic M&A deals have played an increasingly more important role, as well as reduced greenfield FDI performance (Figures 1.6-1.7). Still, inward FDI flows continue to play a larger role in the Kazakh economy than they do in other CIS countries (Figure 1.A1.3 in Annex 1.A1) and, thus far, remain positive, which means that net divestment is not observed. The value of investments by foreign firms via M&A also outweighs the value of foreign M&A divestures (Figure 1.A1.4 in Annex 1.A1). According to the Kazakhstan's national statistical office, as of today, foreign enterprises operating in the country account for 61% of industrial output, 66.2% of total exports, and 5.4% of total employment.

Figure 1.6. **Cross-border and domestic M&A activity in Kazakhstan, 1995-2015**



Note: Deals are identified as cross border when the target and the acquirer are of different nationality.
Source: OECD calculations using Dealogic M&A data.

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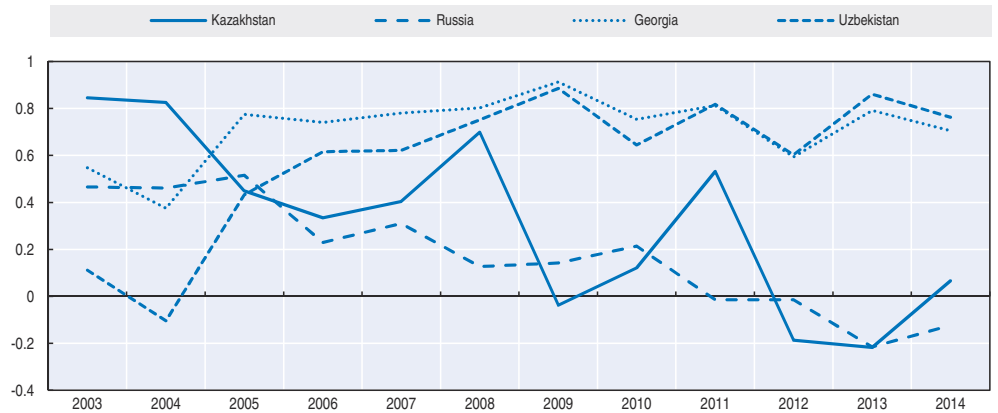
Figure 1.7. **Greenfield FDI Performance Index, 2003-14**



Note: The Index is calculated as a share of country's GDP in the world's GDP divided by the country's share in the world's announced greenfield FDI (normalised around 0). A value > 0 means that a country attracts more FDI than predicted by the size of its GDP.
Source: OECD calculations based on World Bank's World Development Indicators and UNCTAD's World Investment Report.

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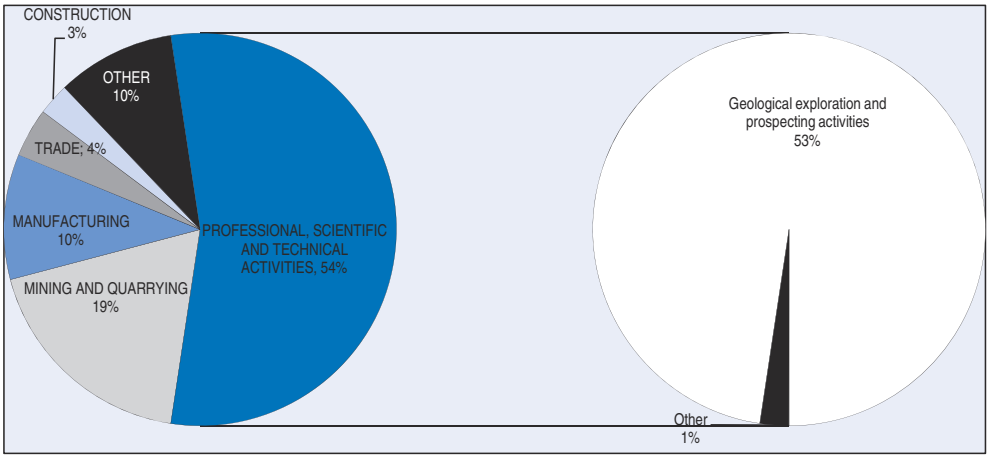
FDI by sector

With its large oil and mineral deposits (IEA, 2015), Kazakhstan has historically attracted significant amounts of FDI into its oil and gas sector. Already in the early stages of its independence in 1990s, the sector attracted foreign entrants, including Chevron, Lukoil, Texaco and Canadian Hurricane

Hydrocarbons Ltd (Peck, 2002). Today, geological exploration and prospecting activities account for 53% of inward FDI stock, i.e. 72 billion USD (Figure 1.8), followed by mining and quarrying (19%). Most of global market players in the sector are present in Kazakhstan, including Chevron, BP, Exxon, Royal Dutch Shell, and Total, and foreign-owned firms, including joint ventures, dominate the sector.[2] The high concentration of FDI in extractives sector also influences the country's trade structure, whereby the country exports primarily fuel to the EU (about 40 billion USD annually) and imports machinery and equipment from the EU (for the use in extractives) as well as refined oil from CIS countries (Figures 1.A1.6 and 1.A1.7 in Annex 1.A1). Kazakhstan still records some FDI in its manufacturing sector (10%), the majority of which is directed at the basic and fabricated metal products sector (84%), followed by food products and tobacco (7%). Most recently, the FDI inflows into the oil and the associated architectural, engineering and technical services sectors have shrunk, reflecting the economic difficulties related to lower oil prices (Figure 1.9). The cross-border M&A activity in the oil and gas sector also declined (from 74% in 1996-2001 to 50% in 2008-15), but jointly with mining still accounts for over two thirds of total M&A deal value in the country (Figure 1.A1.5 in the Annex to this chapter).

Figure 1.8. **Inward FDI stock in Kazakhstan, 2015**



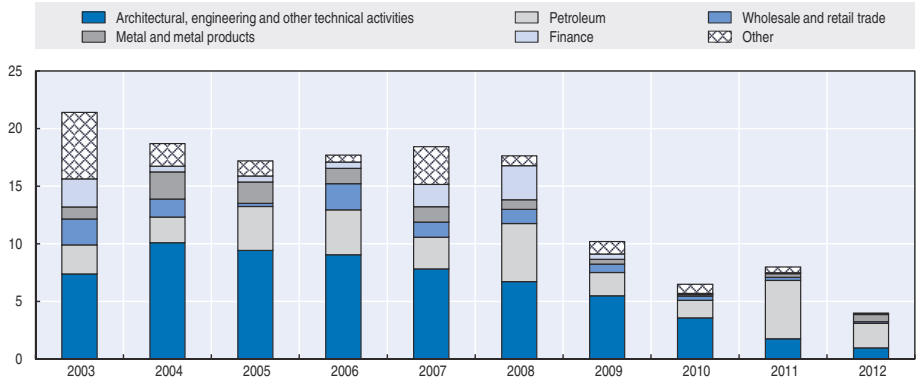
Note: Data as of as of 30/06/2015.
Source: National Bank of Kazakhstan.

StatLink http://dx.doi.org/10.1787/888933452714

FDI by country of origin

According to Kazakhstan's FDI statistics, the EU is by far the most important foreign investor in Kazakhstan, followed by the United States, Japan, the People's Republic of China (China), and Russia (Table 1.1). It is worth noting, however, that the Netherlands, a country with significant share of resident

Figure 1.9. **FDI inflows in Kazakhstan by sector, 2003-12**



Source: UNCTAD, National Bank of Kazakhstan.

StatLink http://dx.doi.org/10.1787/888933452726

Table 1.1. **Inward and outward FDI positions in Kazakhstan, by main partner country, 2015**

Panel A

Liabilities			
Country	In bln USD	Share of total %	Rank
Netherlands	67.00	50	1
United States	19.71	15	2
France	11.64	9	3
Japan	5.14	4	4
United Kingdom	4.82	4	5
Switzerland	3.87	3	6
China	3.57	3	7
Russia	3.54	3	8
British Virgin Islands	2.15	2	9
South Korea	1.49	1	10

Panel B

Assets			
Country	In bln USD	Share of total %	Rank
Netherlands	16.50	51	1
United Kingdom	7.47	23	2
Singapore	1.05	3	3
Luxemburg	1.05	3	4
Russia	0.99	3	5
Switzerland	0.88	3	6
United States	0.83	3	7
British Virgin Islands	0.48	1	8
Turkey	0.38	1	9
UAE	0.38	1	10

Note: Data as of as of 30/06/2015.
Source: National Bank of Kazakhstan.

StatLink http://dx.doi.org/10.1787/888933453052

special purpose entities (SPEs), accounts for a lion's share of both Kazakhstan's inward and outward FDI. This phenomenon reflects the growing difficulty of capturing accurately the true origin of investment, which is channelled increasingly through holding companies and other corporate structures used for purposes of tax or other reasons (OEDC, 2015). An increasing number of countries, including Netherlands, report their FDI statistics with a breakdown of investment undertaken by resident SPEs and non-SPEs (see Box 1.2 for more detail). The OECD home-country FDI statistics confirm that nearly 80% of inward FDI from the Netherlands in Kazakhstan comes from resident SPEs (Table 1.A1.1 in the Annex). Most of Kazakhstan's outward FDI is located in resident SPEs as well, as discussed next. This highlights the importance of improving the methodology for compiling domestic FDI statistics to discern better the true origin and destination of investment as well as suggests that some of the inward FDI in Kazakhstan may in fact be domestic investment channelled through holding companies located abroad, and *vice-versa*, complicating the understanding of the underlying investment trends.

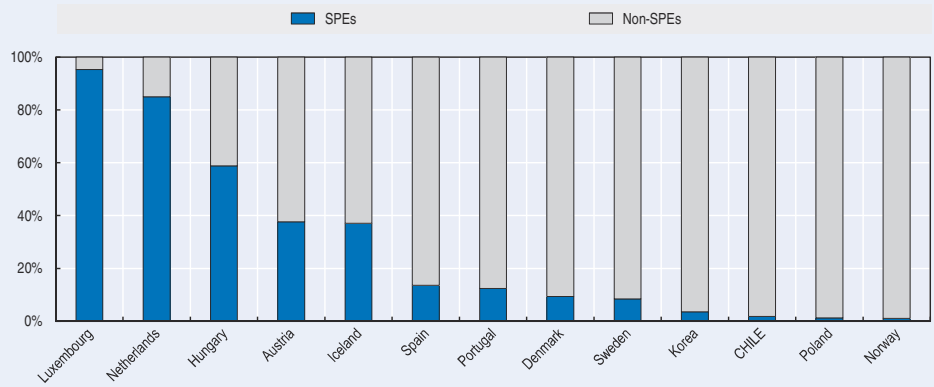
Box 1.2. **Special purpose entities: why do they matter for FDI statistics?**

Special purpose entities (SPEs) also called shell or shelf companies are companies that do not have substantial economic activity in the country but are used by companies as devices to raise capital or to hold assets and liabilities. With the proliferation of international activities and increase in intra-frim trade, including in intangibles, it has become increasingly easy for companies to shift profits across jurisdictions according to the most favourable tax environment through corporate structures built for that purpose. Just as gross trade flows may obscure the destination and origin of value-added produced in a given economy due to multiple shipments of goods across borders during the production process that spans several countries, so the passing of funds through SPEs can lead to the inflation of FDI statistics and the obscuring of the ultimate source and destination of FDI.

The OECD *Revised Benchmark Definition of Foreign Direct Investment* (BMD4) recommends that countries compile their FDI statistics excluding resident SPEs, and, then, separately for resident SPEs to provide a more meaningful measure of direct investment into and out of an economy. For the country hosting the SPEs, this recommendation improves the measurement of FDI by excluding inward FDI that has little or no real impact on their economies and by excluding outward FDI that did not originate from their economies. Four countries – Austria, Hungary, Luxembourg, and the Netherlands – have reported FDI flows and positions excluding resident SPEs to the OECD for several years. With the implementation of the latest standards, 9 additional countries – including Chile and eight other countries[3] – have now reported data excluding resident SPEs. Inward investment positions are the value of the accumulated stock of foreign investment in a host country. Figure 1.1 shows the percentage of inward positions accounted for by resident SPEs in 2013. The countries are displayed according to share of investment accounted for by resident SPEs.

Box 1.2. **Special purpose entities: why do they matter for FDI statistics?** *(cont.)*

Inward FDI positions by resident SPEs and non-SPEs in selected OECD countries, 2013



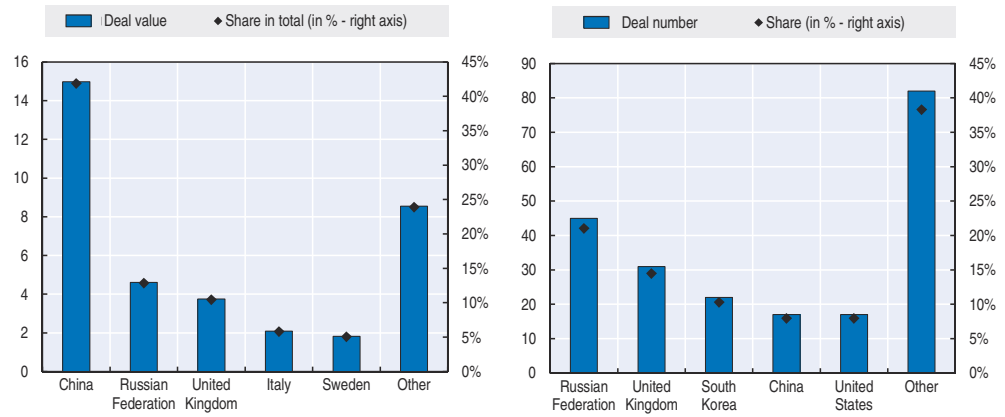
Source: OECD International Direct Investment statistics and IMF.

Even in countries where SPEs do not play a significant role in FDI currently, it is useful to be able to identify resident SPEs in the statistics so that their role in FDI can be monitored. By their nature, SPEs can be formed easily and can grow rapidly. In addition, SPEs can have large transactions in a particular period that can distort FDI flows due to their role within the MNE of providing financing or holding assets and liabilities. By compiling FDI statistics that exclude resident SPEs, FDI statistics are not overstated by including funds that are simply being channelled through the SPEs, are easier to interpret for policy-making and other purposes, and provide a better measure of FDI that is likely to have an economic impact in the host economy.

Source: OECD. For more information, see the OECD website on International Investment Statistics: *www.oecd.org/daf/inv/investment-policy/oecdimplementsnewinternationalstandardsforcompilingfdistatistics.htm*

Other sources of information provide additional insights on the activity of foreign firms in Kazakhstan. For example, information on the operations of foreign affiliates of multinational firms[4] suggest that the largest number of foreign affiliates operating in Kazakhstan stem from the United States (22%), followed by Germany (16%) and the United Kingdom (12%). These companies include many of the Global Fortune 500 and other large TNCs.[5] According to merger and acquisitions (M&A) data, in turn, foreign investors from the Russian Federation, the United Kingdom and the United States have engaged in the largest number of cross-border M&A deals in Kazakhstan in the past fifteen years; while investors from China, the Russian Federation and the United Kingdom have been most important in terms of the total registered deal value (Figure 1.10).

Figure 1.10. **Top five cross-border M&A investors in Kazakhstan by nationality of the acquirer, 1995-2015**



Note: Acquirer nationality is defined to mean the country where the acquirer is either headquartered or has the majority of its managerial operations in.
Source: OECD calculations using Dealogic M&A data.

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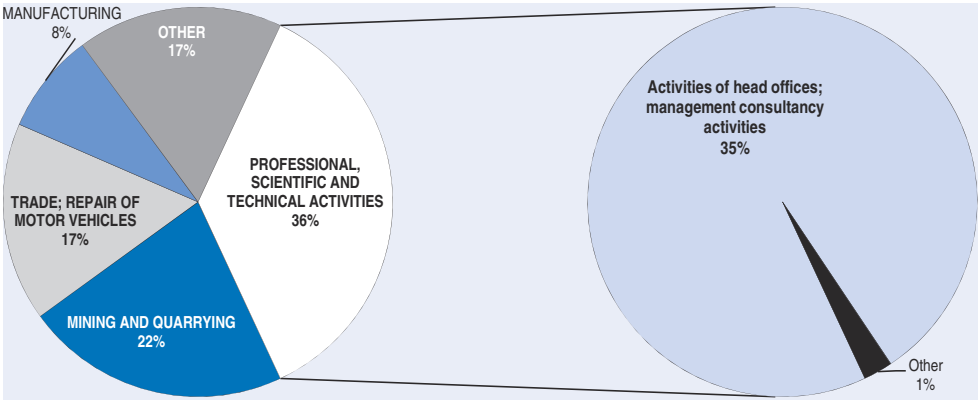
Outward investment

As mentioned earlier, the investments of foreign companies in Kazakhstan outweigh the investments of Kazakh companies abroad. Outward FDI stock (of USD 26.1 billion in 2015) accounts for 12% of GDP, and outward FDI flows (of USD 2 billion in 2015) for 2% of GDP. Also, most of Kazakh outward FDI is directed into head offices and management consulting services (Figure 1.11), which suggests that some of that investment may be investment round-tripping for tax or other purposes. Kazakhstan's outward FDI stock may hence be even lower than suggested by the official statistics. Nevertheless, there are examples of several active investment projects by Kazakh enterprises abroad, including investments by state oil company KazMunayGas in the Rompetrol Group refinery in Romania worth USD 3.8 billion[6] and smaller investments by trade companies, banks, and other financial institutions in the Russian Federation, Turkey, the Kyrgyz Republic, and other countries (Eurasian Development Bank, 2013; Asian Development Bank Institute, 2014).

FDI has played an important role in Kazakhstan's modern history, accounting for about 50% of the country's GDP throughout the 2000s. Some Kazakh companies, in particular state-owned enterprises (SOEs), are also active abroad. Most recently, Kazakhstan has encountered some difficulties in attracting FDI, primarily due to lower global commodity prices as well as consequences of the global financial crisis. In some sectors, in particular in banking, there have been departures of several large global players. Still, on average, foreign firms invest more than they divest in Kazakhstan (i.e. the net

Figure 1.11. **Outward FDI stock in Kazakhstan, 2015**



Note: Data as of 30/06/2015.
Source: National Bank of Kazakhstan.

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investment-divestment ratio remains positive), and, according to business surveys, the country remains an attractive place to invest in the region (EY, 2016). While reasons behind firms' investment and divestment decisions are often diverse and may lie outside of the scope of policy action, the strength of the local business climate and proactive investment attraction policy can be important factors. The following chapters discuss different aspects of investment climate in Kazakhstan and consider how the country could improve its policy framework for investment to retain and attract FDI, including in non-traditional sectors.

Notes

1. The data on value added presented here have been provided by the government. The integration of Kazakhstan into the OECD's statistical systems, including the OECD National Accounts data and Trade in Value Added database would help ensure that the country's national statistics are consistent with those of other countries. Kazakhstan is currently being integrated into the OECD Trade in Value Added database, and the results should become publically available at the time of the next release of the database in 2017.
2. According to the Statistical Office of Kazakhstan, joint ventures accounted for 83% of all firms operating in the sector in 2012.
3. Denmark, Iceland, Norway, Poland, Portugal, Spain, Sweden and the United Kingdom.
4. Information comes from the Investment Map database maintained by the International Trade Center (ITC). The Investment Map database integrates FDI databases developed by UNCTAD, the UN trade database (COMTRADE), tariff databases developed by ITC, and company databases maintained by Dun & Bradstreet. For more information, please see: *www.investmentmap.org/datasource_limit.aspx*.

5. These include, among others, Intel, Microsoft, Procter and Gamble from the United States; Siemens, Deutsche Post and Deutsche Bank from Germany; Royal Dutch Shell PLC, BP PLC; Toyota from Japan; or PSA Peugeot Citroën and Danone from France. Information based on the Investment Map available on the website of the International Trade Center (*www.investmentmap.org*) and embassies of the OECD countries.
6. Information provided by the Government of Kazakhstan.

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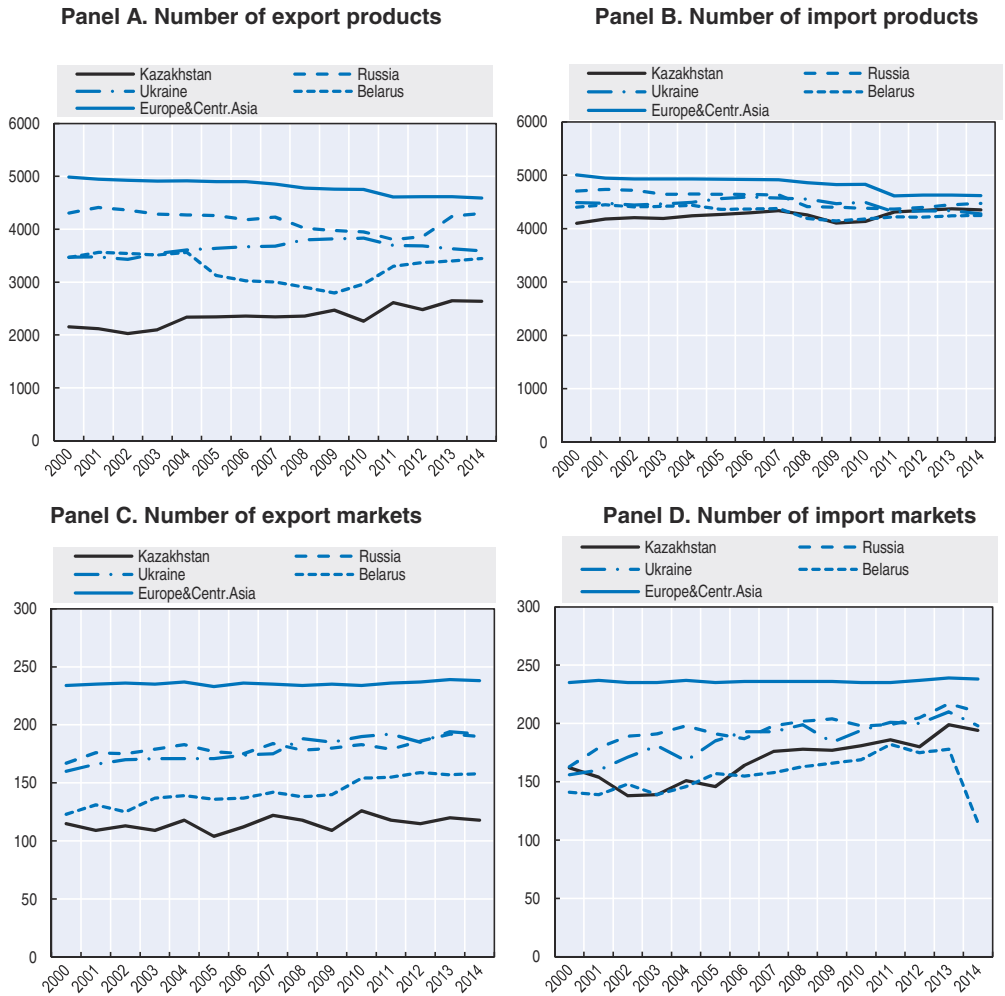
ANNEX 1.A1

Figure 1.A1.1. **Number of export (import) markets and products in Kazakhstan and selected CIS countries, 2000-14**



Source: WITS database.

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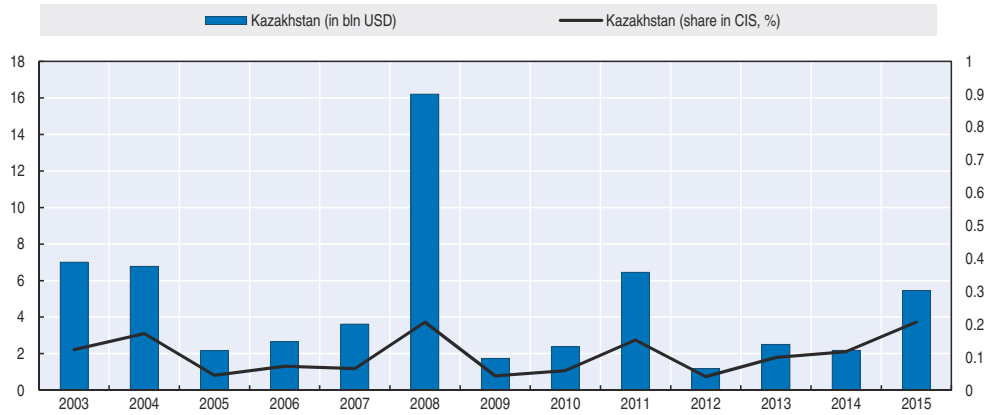
Figure 1.A1.2. **Announced greenfield FDI in Kazakhstan, 2003-14**



Note: Greenfield FDI refers to cross-border investment in a new physical project or expansion of an existing investment which creates new jobs and capital investment, as identified in the FDI markets database of the Financial Times used in the UNCTAD Investment Report. Projects that are below the 10% foreign ownership threshold applied in the official definitions of FDI may also be included.

Source: OECD calculations based on the Word Bank's World Development Indicators and UNCTAD's World Investment Report.

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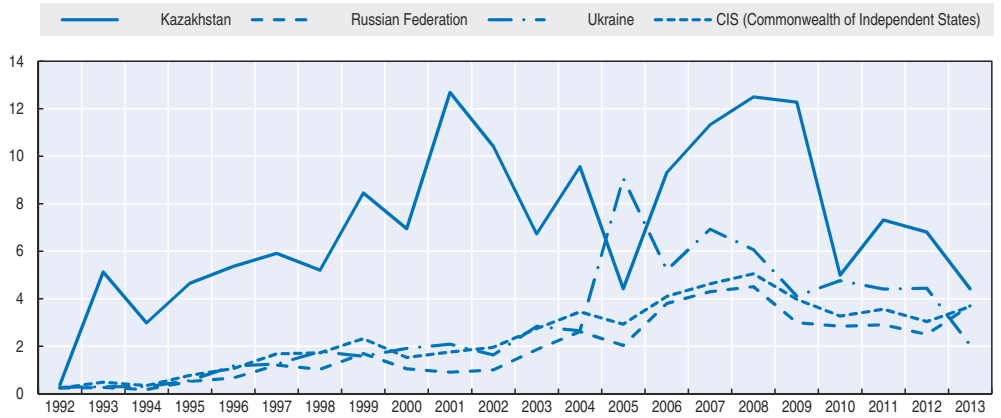
Figure 1.A1.3. **Share of FDI inflows in GDP in Kazakhstan and selected CIS countries, 1992-2013.**



Source: World Development Indicators and UNCTAD.

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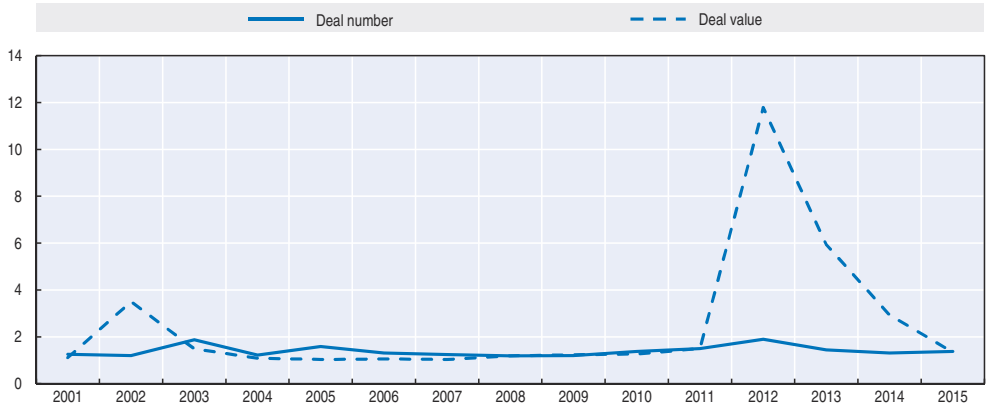
Figure 1.A1.4. **The ratio of foreign acquisitions to foreign divestures in Kazakhstan, 2001-15.**



Source: OECD calculations using Dealogic M&A data.

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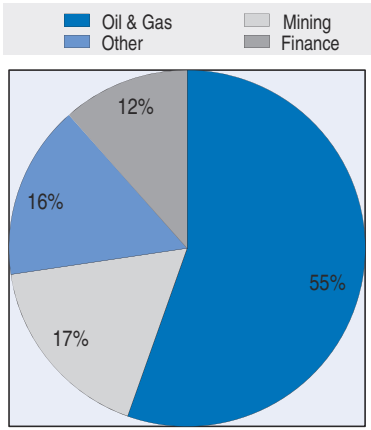
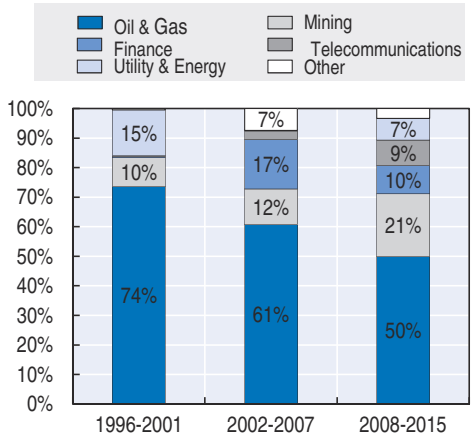
Figure 1.A1.5. **Sectoral distribution of M&A activity in Kazakhstan, 1995-2015.**

Panel A. Total deal value (in %, 1995-2015)



Panel B. Total deal value over time (in %)



Source: OECD calculations using Dealogic M&A data.

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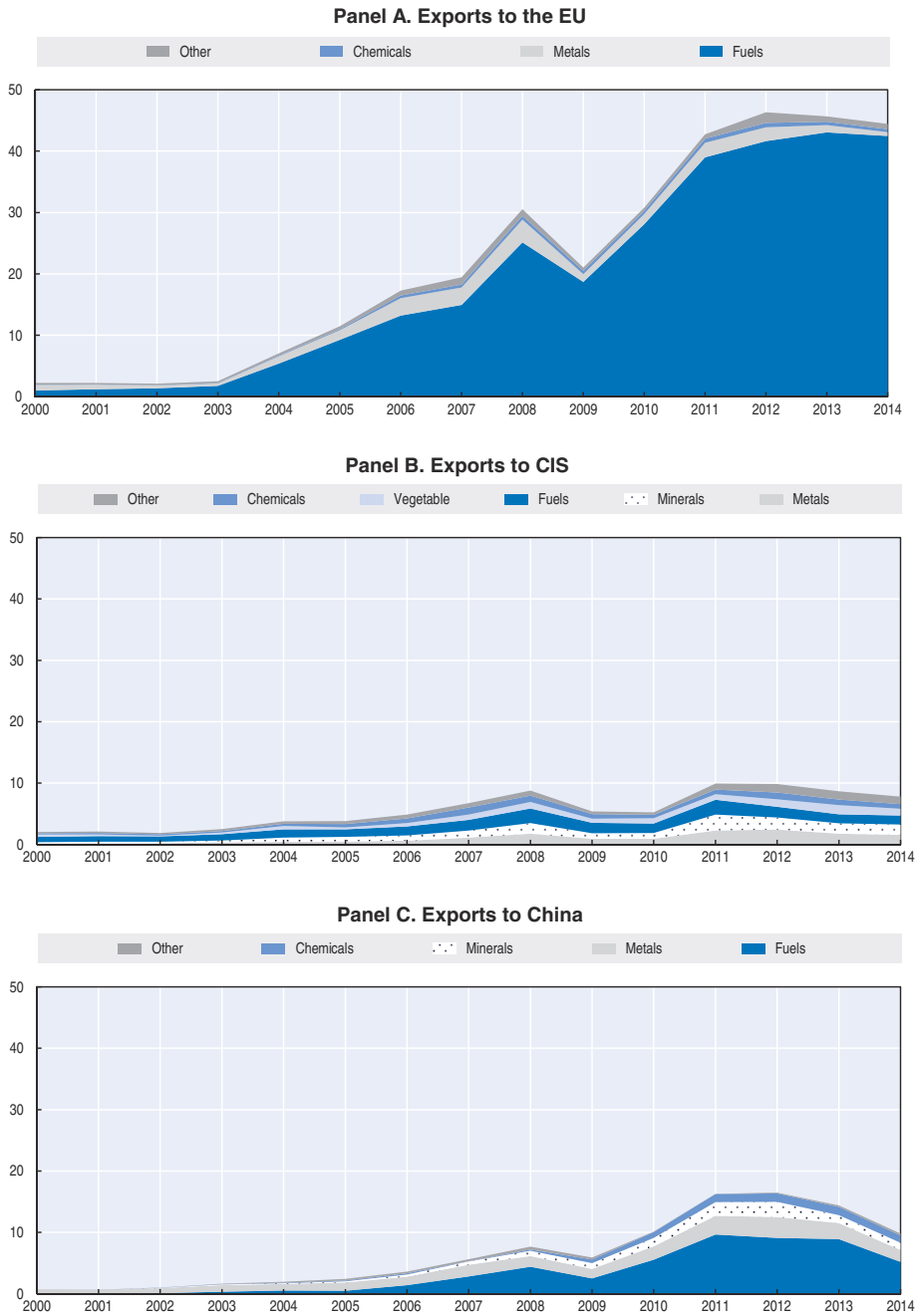
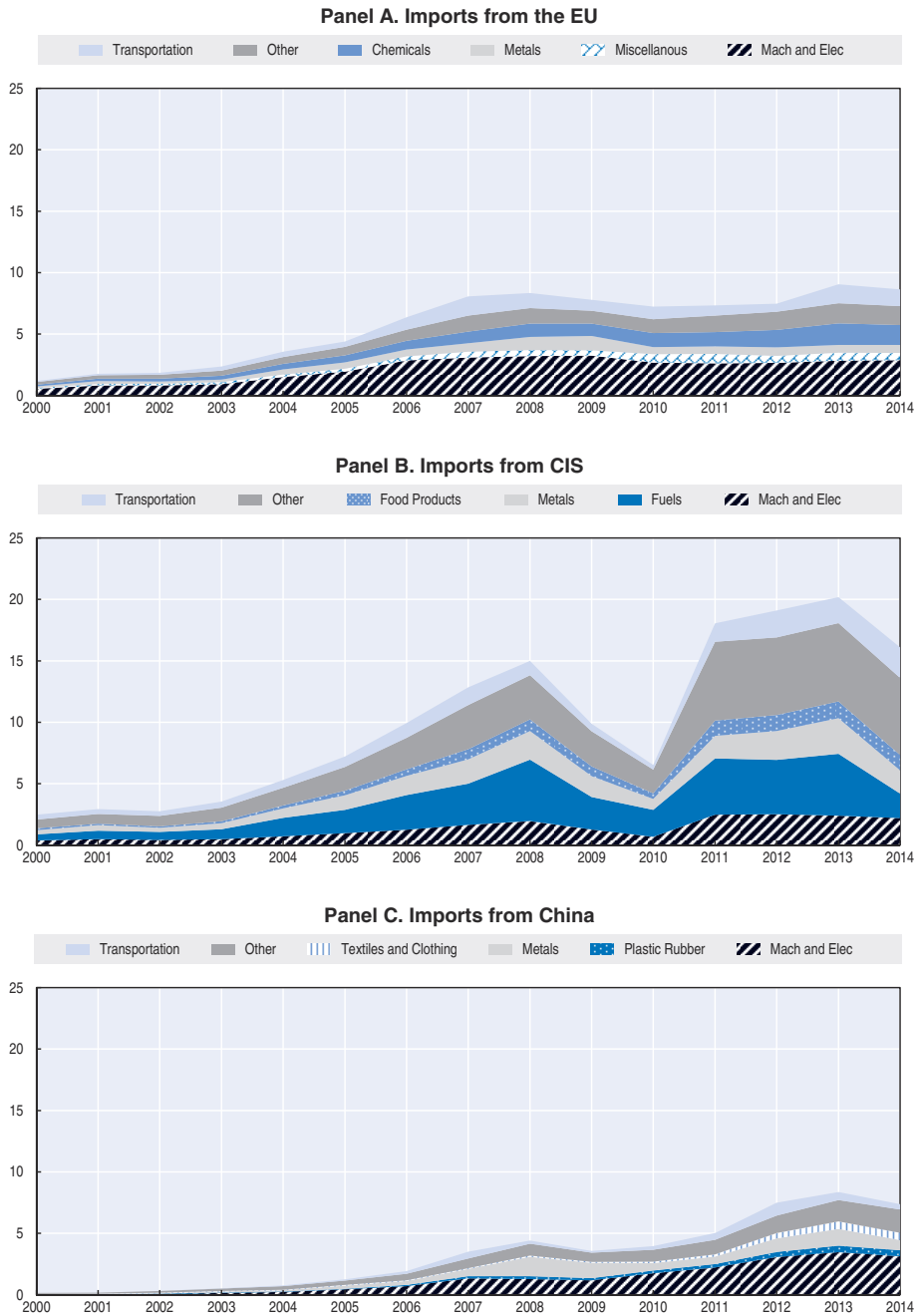
Figure 1.A1.6. **Kazakhstan's export structure with the main trading partners, 2000-14**



Source: UN COMTRADE.

StatLink http://dx.doi.org/10.1787/888933452797

Figure 1.A1.7. **Kazakhstan's import structure with the main trading partners, 2000-14**



Source: UN COMTRADE.

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Table 1.A1.1. **FDI positions of OECD countries in Kazakhstan, 2014**

In bln USD

Panel A. Outward positions of OECD countries			
Reporting country	All resident units	Resident SPEs	Resident Non-SPEs
Netherlands	44.5	34.7	9.9
United States	15.6	0.0	15.6
United Kingdom	4.5	0.0	0.0
Canada	2.7	0.0	0.0
Italy	0.7	0.0	0.7
Turkey	0.4	0.0	0.4
Poland	0.1	0.0	0.1
Panel B. Inward positions of OECD countries			
Type of entity	All resident units	Resident SPEs	Resident Non-SPEs
Netherlands	-0.1	0.1	0.0
United States	0.0	0.0	0.0
Poland	0.0	0.0	0.0
Italy	0.0	0.0	0.0
Hungary	0.0	0.1	-0.1
Estonia	0.0	0.0	0.0
Czech Republic	0.0	0.0	0.0
Turkey	0.3	0.0	0.3
Netherlands	-0.1	0.1	0.0

Source: OECD International Investment database.

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Table 1.A1.2. **Top 10 M&A deals involving a target firm from Kazakhstan, 1995-2015**

	Completion Date	Acquiror Nationality	Acquiror	Acquiror Parent	Divestor Nationality	Divestor	Deal value (mln USD)	Target	Target Sector
1	31-Oct-13	Kazakhstan	National Co KazMunaiGas ZAO	National Co KazMunaiGas ZAO	United States	ConocoPhillips	5 400	Oil and Gas Assets (Kashagan field in Kazakhstan)	Oil and Gas
2	04-Nov-13	China	China National Petroleum Corp – CNPC	China National Petroleum Corp – CNPC	Kazakhstan	National Co KazMunaiGas ZAO	5 000	Oil and Gas Assets (Offshore oilfield in the Caspian Sea)	Oil and Gas
3	31-Aug-10	Kazakhstan	Creditors	Creditors			4 989	BTA Bank AK (18.5%)	Commercial Banking
4	22-Oct-15	Kazakhstan	Samruk-Kazyna JSC	Samruk-Kazyna JSC	Kazakhstan	National Co KazMunaiGas ZAO	4,700	KMG Kashagan BV (50%)	Oil and Gas
5	26-Oct-05	China	China National Petroleum Corp – CNPC	China National Petroleum Corp – CNPC			4 180	PetroKazakhstan Inc	Oil and Gas
6	06-Aug-15	Kazakhstan	Market Purchase	Market Purchase	Kazakhstan	Samruk-Kazyna JSC	3 979	National Co KazMunaiGas ZAO (10%)	Oil and Gas
7	25-Nov-09	Kazakhstan	National Co KazMunaiGas ZAO; China National Petroleum Corp – CNPC	National Co KazMunaiGas ZAO; China National Petroleum Corp – CNPC	Indonesia	Central Asia Petroleum Ltd	3 300	Mangistaumunaigaz AO	Oil and Gas
8	28-Jun-12	Kazakhstan	National Co KazMunaiGas ZAO	National Co KazMunaiGas ZAO	United Kingdom	BG Group plc; LUKOIL-AIK ZAO; Chevron Corp; ENI SpA	3 000	Karachaganak Petroleum Operating BV (10%)	Oil and Gas
9	23-Jul-08	Kazakhstan	Kazakhmys plc	KAZ Minerals plc	Kazakhstan	Republic of Kazakhstan	2 253	Eurasian Natural Resources Corp – ENRC (7.66%)	Mining
10	25-Oct-13	Kazakhstan	Eurasian Resources Group BV; Private Investor; Ministry of Finance of the Republic of Kazakhstan; Samruk-Kazyna Sovereign Wealth Fund AO	Eurasian Resources Group BV; Private Investor; Republic of Kazakhstan; Samruk-Kazyna JSC	Kazakhstan	Kazakhmys plc (26%)	2 097	Eurasian Natural Resources Corp – ENRC (45.0569%)	Mining

Source: OECD calculations using Dealogic M&A data.

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Chapter 2

Kazakstan's investment regime

Kazakhstan has been determined to make the regulatory framework more conducive to foreign investment. Reforms have resulted in the removal of obstacles to FDI so that foreign investors can now participate in almost all sectors of the national economy on an equal footing with domestic investors. While Kazakhstan is getting closer to OECD levels in terms of statutory restrictions according to the OECD FDI Regulatory Restrictiveness Index, some sectoral restrictions are still posing constraints on investment. Remaining restrictions include mass-media, where equity limits apply; fixed-line telecommunications, where authorisation is required for foreign participation above a certain threshold; security services, where foreign investment is prohibited; and the use of agricultural forestry and land. Kazakhstan also maintains somewhat burdensome conditions with regards to the employment of key foreign personnel, which apply horizontally across economic sectors, and are relatively less typical among OECD countries. Other investment impediments include the weight of the public sector in the national economy. The share of state-owned enterprises in the economy should nevertheless decrease to 15% by 2020 against over 35% in 2016.

The enabling environment for investment faced by foreign investors, both when they first establish and in their on-going operations, is a key component of the OECD *Declaration on International Investment and Multinational Enterprises*. The *Declaration* consists of OECD instruments designed to promote international investment in a transparent and responsible manner. Under the *Declaration*, governments voluntarily commit to a balanced set of rights and obligations for foreign investors through in particular the *National Treatment* instrument and the *Guidelines for Multinational Enterprises*. This chapter examines Kazakhstan's investment regime in light of the *National Treatment* instrument, the first element of the *Declaration,* which establishes an internationally recognized standard of treatment that helps eliminate discrimination vis-à-vis foreign controlled enterprises operating in the territories of Adherents (Box 2.1). Kazakhstan's framework regarding investment incentives is further analysed in Chapters 4 and 5, whereas Kazakhstan's framework for responsible business conduct, as covered by the *Guidelines for Multinational Enterprises*, is analysed in Chapter 7.

Box 2.1. **The OECD Declaration on International Investment and Multinational Enterprises**

Adopted in 1976, the *Declaration* is a policy commitment by Adherents to provide an open and transparent environment for international investment and to encourage the positive contribution multinational enterprises can make to economic and social progress.

The *Declaration* consists of four main elements:

- ***National Treatment:*** A voluntary undertaking by Adherents to accord to foreign-controlled enterprises established on their territories treatment no less favourable than that accorded to domestic enterprises in the same situations.
- ***The Guidelines for Multinational Enterprises:*** Recommendations on responsible business conduct addressed by governments to multinational enterprises operating in or from Adherents. The *Guidelines* were updated in 2011.
- ***Conflicting requirements:*** Adherents agree to co-operate so as to avoid or minimise the imposition of conflicting requirements on multinational enterprises.

Box 2.1. **The OECD Declaration on International Investment and Multinational Enterprises** *(cont.)*

- ***International investment incentives and disincentives:*** Adherents recognize the need to give due weight to the interest of other adhering countries affected by laws and practices in this field; they need to strengthen international co-operation in this area and endeavour to make measures as transparent as possible.

All 35 OECD member countries have adhered to the *Declaration*, as have 12 non-member countries: Argentina (22 April 1997), Brazil (14 November 1997), Colombia (8 December 2011), Egypt (11 July 2007), Lithuania (20 September 2001), Morocco (23 November 2009), Peru (25 July 2008), Romania (20 April 2005), Tunisia (25 May 2012), Costa Rica (30 September 2013), Jordan (28 November 2013), and Ukraine (15 March 2017).

Main features of Kazakhstan's investment regime: Overall policy approach towards foreign investment

The authorities have made strides in opening the country to international investment. Foreign investors can participate in most sectors of the economy on an equal footing with domestic investors. The government notably recently lifted the previous equity restriction in air transport and prohibition of foreign capital above a certain threshold in telecommunications. Kazakhstan's score in the OECD FDI Regulatory Restrictiveness Index (a measure of statutory restrictions on foreign direct investment) is getting closer to OECD levels, although it is above the OECD average. Additional changes, expected to be implemented within five years of Kazakhstan's 2015 accession to WTO, should support an even more open environment for foreign investors.

Ground-level conditions are nevertheless still posing constraints on investment, despite recent and on-going steps to eliminate some of them. The main operational restriction on foreign investment, primarily in the energy and mining industries, has involved a local content requirement covering goods and services, as well as labour. Since Kazakhstan's accession to WTO, the government has started to reduce local content requirements and it is expected that at the end of a five-year transition period (i.e. by 2021), they will be further reduced. Reforms undertaken by Kazakhstan in this area are described in the section below on horizontal policies affecting FDI.

Other investment impediments include the weight of the public sector in the national economy. In spite of extensive privatisation in the 1990s and 2000s, the state is still heavily present, making up between 35% and 40% of the national economy according to some estimates. Also, a vast range of important industries and economic sectors are natural monopolies in Kazakhstan: some 1 200 companies

in 15 spheres of economic activity in 2016. The excessive market power of some of these companies may have adverse consequences for the overall competiveness of the economy and a negative impact on foreign investment. Recent initiatives have nevertheless focused on reducing the share of SOEs in the economy: the on-going privatisation plan for 2016-20 aims at reducing the so-called quasi-state companies owned by the central government to 15% by 2021. Other reforms aimed at encouraging competition and entry and operations of investors in activities formerly reserved to monopolies are underway.

Horizontal policies affecting FDI

Many resource-rich countries have put in place, at one point or another in the course of their development path, specific policy instruments requiring firms to use domestically available factors of production in an attempt to derive more benefits from their resource endowments. It is estimated that still today over 90% of these countries –and this includes OECD countries– have one form of local content policy or another as regards their extractive industries (Korinek et al., forthcoming). Kazakhstan is not an exception. Local content requirements, which also apply to labour, have long been seen by the Kazakh authorities as a way of building domestic supply capacity and spreading the benefits of the economic boom, especially the natural resource one. In the framework of its 2012 *Review* of Kazakhstan the OECD nevertheless noted that Kazakhstan's local content policy significantly added to the administrative burden on an enterprise's operations and to the cost of doing business in Kazakhstan (OECD, 2012). Since then, in connection with its accession to the WTO, the country has started to adopt new legislation and regulation aimed at altering or phasing out some existing requirements, including with regards to foreign labour and key personnel.

Labour policy

Kazakhstan's local content policy applies to labour, combined with rather stringent rules on hiring foreign labour, including key personnel. Employers, in order to engage foreign labour and foreign workers, are required to obtain permits within a quota established by the government.[1] In 2016, the quota made up 0.7% of Kazakhstan's economically active population (i.e. 60 000 individuals). Work permits restrictions do not apply in certain cases, including: nationals of the State Parties to the Eurasian Economic Union Treaty (citizens of Armenia, Belarus, Kyrgyzstan and Russia); top management positions in branches and representative offices; chief executive officers (CEOs) in companies concluding contracts of over USD 50 million; managers in firms active in priority investment activities; and managers of Kazakh legal entities which have signed investment contracts for the implementation of an investment priority project. In 2016, they also were not applied for the hiring of

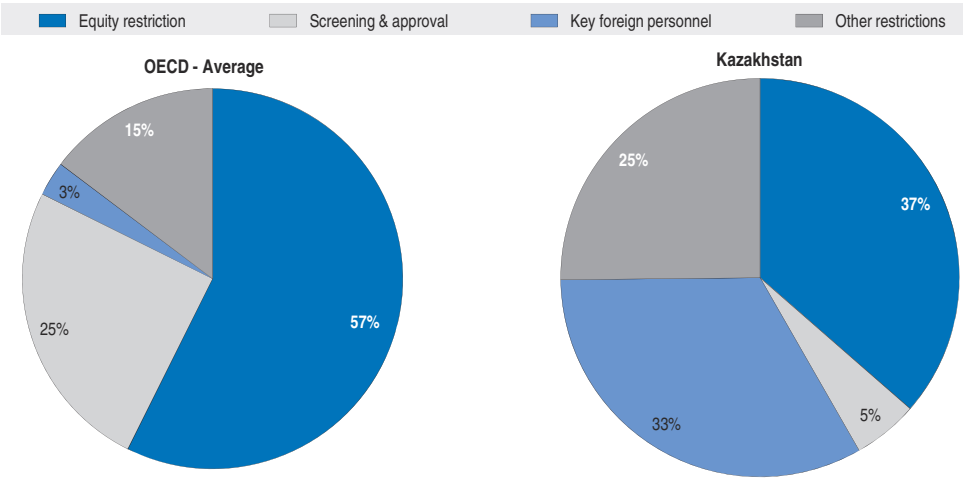
managers and specialists in the "Park of Innovative Technologies" Special Economic Zone.[2]

Beyond these exceptions, restrictions apply to all employee categories. There are 4 categories of employees for which a working permit is required: Category I, which includes chief officers and their deputies; Category II, which deals with managers and specialists; Category III, which concerns technical experts; and Category IV, which comprises qualified workers. Restrictions vary according to the category of employees. Pursuant to a Government Resolution from 2012[3] which somewhat tightened the rules governing work permits, foreign staff are limited to 30% of Category I (against 50% in 2011) and of Category II. In the other two categories (specialists and qualified workers), foreign staff are limited to 10%.

The duration of work permits also varies from one category to another. Work permits are generally offered for one year, for categories II, III and IV, with the possibility of an extension for at most 2 years for categories II and III but not for category IV (qualified workers). Work permits for category I workers (executives and their managers) are offered for up to 3 years and can be extended for up to 12 months an unlimited number of times. Until the beginning of 2017, a labour market test (also called Economic Needs Test) was a prerequisite to receiving a work permit: the authorities would consider a work permit application only if there were no local employees qualified for the vacancy. In order to obtain work permits, employers had also to comply with "special conditions", i.e. provide advanced training to Kazakhstani employees and/or create additional jobs for Kazakh citizens, as determined by local authorities.

In its first *Review* of Kazakhstan, the OECD noted that hiring expatriate staff involved a cumbersome process, and restrictions concerning the share of foreign staff existed in almost each type of position (OECD, 2012). In 2014, this horizontal restriction on the movement of people and key foreign personnel still accounted for one third of Kazakhstan's overall score on the FDI Regulatory Restrictiveness Index, in contrast with OECD economies where such restrictions are less typical (Figure 2.1). Foreign investors have been complaining about the difficulties in hiring foreign labour for most of the past decade. Kazakhstan's visa policy has also been seen as presenting an unnecessary obstacle to investors. Perhaps illustrative of this, national statistics on the number of work permits granted in the period 2013-15 show that the number of delivered work permits never matched the annual quota: in 2015, only 33 500 work permits were granted for 63 000 available (i.e. about 53%); in 2013, of a quota of over 100 000 individuals who could obtain a work permit, the number of issued permits did not exceed 26 000 (i.e. 25%).[4] It would appear that locally-established foreign investors as well as domestic entrepreneurs might have decided to stay away from processes that have been perceived as time-consuming and document-intensive.

Figure 2.1. **FDI Regulatory Restrictiveness Index in Kazakhstan and other economies, by restriction type, 2014**



Source: OECD FDI Regulatory Restrictiveness Index (2014).

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As mentioned above, Kazakhstan has committed to introduce changes in relation to the hiring of foreign workers as part of its obligations under GATS. As part of this process, in September 2015, the authorities removed the "special conditions" (or extra recruitment obligations) on companies hiring foreign managers and directors (the so-called "first category" employees), which included requirements for training and hiring of local workers.[5] In November 2015, changes were made to the conditions and procedure for issuing and extending foreign labour engagement permits in the framework of intra-corporate transfer.[6] Such a transfer can now be performed for a period of up to 3 years (with a year prolongation as an option). Furthermore, while foreign labour work permits are issued within the quota determined each year by the government, the quota does not apply to foreign staff engaged in the framework of intra-corporate transfers (ICTs). The number of such "transferred" employees to Kazakhstan remains nevertheless subject to compliance with the percentage ratio of the number of foreign employees to the number of local employees established by the authorities: their number must not exceed 50% of the total number of managers and specialists within a company. Furthermore, foreign employees may be attracted on an intra-corporate basis only within sectors of the economy determined by the Government.

Other changes were introduced in April 2016 in conjunction with the entry into force of a new employment law.[7] From January 2017 rules governing foreign labour are as follows:

- Annual quotas continue to apply but are now distributed by economic sectors.

- Fees apply to work permits instead of extra recruitment obligations on companies hiring foreign labour.
- The economic needs test (ENT) is no longer required, except in the case of employment of foreign intra-corporate transferees (ICTs) as managers and specialists. Such requirement will continue to apply to this category of employees until 2020 at the latest.[8]

While the measures above can be seen as an effort by the authorities to simplify and improve the procedures for the hiring of foreign labour, other amendments adopted in 2015 and 2016 have somewhat tightened the rules for employing foreign workers. For example, amendments to existing legislation in 2015 have made more complex the rules for companies hiring foreign employees to work in more than one region of Kazakhstan. Previously, foreign staff were able to extend a work permit for one region of the country to another region but now must apply for new work permits for each new region, unless they spend less than 91 days outside the region issuing the permit.[9] Furthermore, although the regulations recently adopted make it easier for local companies to employ foreign managers and directors in the framework of intragroup relocation, companies in Kazakhstan still confront a costly and complicated maze of regulations requiring them to justify why they must hire a foreigner. For example, while the government is committed to eliminate all labour test requirements by 2020, new regulations adopted in March 2016 tightened the rules governing the employer's obligation to conduct a preliminary search for labour on the Kazakhstan labour market in the event of ICTs.[10]

In the same vein, despite Kazakhstan's commitment to introduce changes in relation to the entry and temporary stay of natural persons, including business visitors, as part of its obligations under GATS, the rules and procedures have broadly remained the same, this despite the issuance of a new decree in this regard in April 2016.[11] A maximum period of 120 days per calendar year still applies to business visitors who enter and remain in Kazakhstan without obtaining a work permit.[12] The Government Decrees of March and April 2016 also tightened the rules governing foreigners' stay by requiring host companies to inform the internal affairs authorities about foreign workers staying with them within 3 business days of the date of their arrival.[13] Moreover, in case a foreign worker changes temporary his/her place of residence in the country, both the company and the individual are required to notify the internal affairs authorities within 3 and 5 business days, respectively. The latter has to re-register with the authorities at the place of his/her new residence. Such requirements risk imposing an additional burden on foreign investors. The authorities should ensure that the administrative procedures in this area and in others do not serve as a *de facto* barrier to hiring foreign personnel.

Local content requirements

In addition to tightening the rules governing work permits in the recent past, the Kazakh authorities have until recently increasingly inserted requirements for local content into the country's legal framework through legislation, regulations, contracts and bidding practice, with the overall objective to increase the use of local inputs of goods and service in production by foreign investors in Kazakhstan. This policy has been implemented particularly in the oil, gas and mining sectors, but has covered other sectors as well, such as the automotive industry.

As a result of its accession to WTO in June 2015, Kazakhstan has begun a five-year transition period to bring its local content laws, policies and contracts into compliance with the new WTO requirements. The first legislative amendments adopted in October 2015 primarily concerned the oil and gas sector as regulated by the Law on Subsurface and Subsurface Use of 2010.[14] These amendments entailed introduction of changes in requirements in respect of local content and acquisition of goods, work and services when performing Subsurface use operation contained in the Law on Subsurface and Subsurface Use. The new legislation has also eased in that context the requirements in respect of local staff engagement. In addition, it has abolished preferential treatment given to local producers in procurement of goods and services by state-owned companies.

Pursuant to the amendments to the Law on Subsurface and Subsurface Use, obligations in respect of local content in goods are now excluded from the newly concluded contracts. Previously, subsurface users were required to use "equipment, materials and finished products manufactured in Kazakhstan, provided they meet the requirements of competition and the laws of the Republic of Kazakhstan".[15] The requirement on mandatory use of equipment, materials and finished products manufactured in the Kazakhstan, as well as on mandatory acquisition of the Kazakhstan manufacturers' goods, has now been abolished.[16]

The new legislation adopted in October 2015 also eases the requirements in respect of local staff engagement. Although a subsurface user is still obligated to give preference to local staff in the course of subsurface use operations, this requirement does not apply any longer to managers and specialists hired within the framework of intra-corporate transfers where other conditions apply. In other words, subsurface users are now entitled to use managers and specialist transferred to Kazakhstan as part of an intra-corporate transfer, provided that the number of Kazakh citizens is kept at not less than 50% of the total number of employees in each respective category and that they meet other requirements (see also Chapter 6).[17]

Other requirements that pre-existed to the adoption of the new legislation remain in force however. Acquisition by a subsurface user and its contractors of work and services from Kazakhstan producers and manufacturers remains mandatory for exercising subsurface use right.[18] Although the minimal threshold for services has decreased from 90% in the recent past to 50% in order to comply with the commitments undertaken in WTO's services market access schedule,[19] it may still be perceived by some foreign investors as high.

In addition to local content requirements that apply to procurement of work and services by subsurface users within the framework of investment contracts in the oil and gas and mining sectors, Kazakhstan also applies local content requirements, in the form of preferences for purchase of locally produced goods, under investment agreements in the automotive sector. Such agreements are governed by the Order No. 113 of 11 June 2010 of the Deputy Prime Minister "On Certain Issues on Concluding, Conditions and Model Form of the Agreement on Industrial Assembly of Motor Vehicles with Legal Entities – Residents of the Republic of Kazakhstan". Pursuant to the Order, a company that has signed a contract for industrial assembly of motor vehicles must ensure a local content level of at least 50%. At the time of writing of this *Review*, four companies had concluded agreements on industrial assembly with the Ministry for Investments and Development, two of them dealing with the industrial assemblies of Peugeot and Toyota automobiles. As part of its accession to WTO, Kazakhstan committed that, from 1 January 2015, any new industrial assembly agreements concluded with investors in the automotive sector will not include provisions that are WTO inconsistent. Kazakhstan also committed to eliminate all WTO-inconsistent measures contained in the existing four industrial assembly agreements by 1 July 2018.

Still in order to comply with the WTO provisions, Kazakhstan ended in 2015 its policy consisting of granting preferential treatment for local production and services supplied by domestic firms in the framework of commercial procurement conducted by companies owned or directly or indirectly controlled by the state. Previously, Kazakhstan suppliers of goods, works and services (hereafter: Kazakhstan manufacturers) were granted a putative reduction in the price of their bids during a tender procedure (up to 20% on goods and 10% on works and services). The Law No. 365-V "On Amendments and Addenda to Certain Legislative Acts of the Republic of Kazakhstan Related to the Accession to the World Trade Organisation" of 27 October 2015 has removed the local content provisions in procurement of companies with state participation. As a result of this new legislation, paragraph 5 of Article 19 of the Law "On the National Welfare Fund" (the largest state-owned conglomerate), which gave preference in tender procurements of "Samruk-Kazyna" to domestic firms over both non-resident and locally-established foreign controlled enterprises that did not meet the criteria of "Kazakhstan manufacturers" has been eliminated.

In the same vein, given that all national holdings and national companies are established in Kazakhstan in the form of joint stock companies with state participation, paragraph 2 of Article 34-1 of the Law "On Joint Stock Companies" of 13 May 2003, which provided for similar preferential treatment, has been abolished.

Although valuable, these initiatives appear to be often *ad-hoc* and limited to comply with WTO requirements, without addressing the full set of issues faced by businesses. The promotion of greater domestic involvement should be tackled in a comprehensive manner and not follow a piecemeal approach which may exacerbate many problems already identified at the time of the first *Investment Policy Review*. Alternative measures do exist to empower local labour force or spur the development of domestic supply chains, for example business linkages between domestic and locally established foreign-owned firms and support programmes for SMEs as described in Chapter 5 on investment promotion and facilitation. Local content requirements need to be evaluated against alternative policy options. If some requirements have to be maintained, they should be clearly defined and applied in a transparent and comprehensive manner.

Sectoral policies

The sections below present the exceptions to the OECD *National Treatment* instrument notified by Kazakhstan as well as measures notified by Kazakhstan for transparency purposes as defined by the *Declaration on International Investment and Multinational Enterprises*. The latter measures include restrictions that may be based on national security considerations, others measures reported for transparency such as corporate organisation requirements as well as public and private monopolies and concessions.

Box 2.2. **The OECD National Treatment instrument for Foreign-Controlled Enterprises**

National treatment is the commitment by an Adherent to the *Declaration on International Investment and Multinational Enterprises* to treat enterprises operating on its territory, but controlled by the nationals of another country, no less favourably than domestic enterprises in like circumstances. The *National Treatment* instrument consists of two elements: a declaration of principle, which forms part of the Declaration, and a procedural OECD Council Decision which obliges Adherents to notify their exceptions to national treatment and establishes follow-up procedures to deal with such exceptions. The Decision comprises an annex that lists exceptions to national treatment, as notified by each Adherent and accepted by the OECD Council. The OECD Investment

Box 2.2. **The OECD National Treatment instrument for Foreign-Controlled Enterprises** *(cont.)*

Committee periodically examines the exceptions. Only measures concerning legal entities are reported for the purpose of the National Treatment instrument, and thus any measure that may apply to natural persons is not reflected in the list contained in the annex to the Council's decision. To ensure transparency, Adherents to the Declaration also undertake to report any measures that, while not representing exceptions to national treatment, have an impact on it. The lists of these exceptions and measures are published and regularly updated. There are featured in Annex B to the present *Review*, whereas Annex A presents Kazakhstan's exceptions to national treatment.

Exceptions to the OECD National Treatment instrument notified by Kazakhstan

The exceptions concerning National Treatment notified by Kazakhstan concern the ownership and use of agricultural and forests, security services, fixed-lined telecommunications and mass-media (see Annex A at the end of this *Review*). Although restrictions in fixed-lined telecommunications and mass-media are grounded on national security interests under Kazakhstan's legislation, the Kazakh authorities, showing their willingness to adopt best practices in this area, decided not to record them under the National Treatment instrument under measures noted for transparency based on public order and essential security considerations but instead placed them under the disciplines of National Treatment instrument through adjusting the list of exceptions to the National Treatment instrument accordingly.

Access to agricultural land and forestry

One of the principal objectives of Kazakhstan's authorities since the past decade has been to boost the agricultural sector as part of the strategy for economic diversification.[20] Restricting access to agricultural land can hold back agricultural development and economic diversification (OECD, 2013). In 2012, the OECD recommended Kazakhstan to increase the access to agricultural land and forestry for foreign investors, after having noted that agri-business is a priority sector for diversification and that Kazakhstan had more statutory restrictions on foreign investment in this sector than the OECD average (OECD, 2012).

Restrictions still apply in relation to agriculture and forestry.[21] Only Kazakh citizens and legal entities can own forests. Furthermore, foreign legal entities and subsidiaries of foreign companies, where the share of foreign equity participation is more than 50%, are not allowed to own agricultural land

plots. Foreign land users are also not entitled to permanent land use. They are entitled to lease agricultural land plots and forest service land for up to 10 year years, while Kazakh legal entities can lease agricultural land for up to 49 years. While the government planned to extend the lease period to 25 years for foreign land users, the reform has been stalled due to public protests.[22]

By contrast, foreign nationals and legal entities may hold private ownership of land plots granted for construction, or land plots comprising constructed production and non-production buildings, including residential (structures, facilities) and their complexes, and land designed to serve buildings (structures, facilities) in accordance with the intended use.

Communications technology

The government has been liberalising gradually the telecommunications sector since 2004, replacing the 1999 Telecommunications Law with a new law in 2004. This reduced the market power of the state-owned incumbent operator Kazakhtelecom, primarily on the mobile telephony market. The government has also progressively reduced its share in Kazakhtelecom, until it reached 51% in 2007. Since 2004, foreign investors have entered the sector (Tele2 was the last foreign operator to enter the Kazakh market in 2010), including through the acquisition of Kazakhtelecom's shares in existing local mobile operators.

As a result of this gradual liberalisation, foreign-owned operators now dominate the mobile telephony market,[23] which has thus benefited from technological upscaling and registered years of dynamic growth. Although the mobile segment has now reached saturation (mobile phone penetration reached 170% at the end of 2014), growth potential is strong in mobile data services.[24] By contrast, state-owned Kazakhtelecom controls the lion's share of the fixed-line telephony (now accounting for less than 20% of overall telecom revenues, while the mobile segment accounts for around 50%) and broadband internet market segments. According to its annual report, Kazakhtelecom accounted for 84.5% of broadband internet subscribers and 92.2% of fixed telephony subscribers in 2014. In addition to Kazakhtelecom, two affiliates of other large SOEs (Kaztranskom and Transtelecom) are among service providers of fixed line telephony and broadband internet access. Fixed broadband internet penetration reached 13 per 100 inhabitants in 2014, slightly below the Russian Federation (17 per 100 inhabitants). Given impressive growth (broadband internet penetration was only 5.5 per 100 inhabitants in 2010) in recent years and relatively low penetration level, this segment will remain the most dynamic on Kazakhstan's telecommunication market for the next few years.

Until recently, foreign individuals and legal entities could not directly or indirectly possess more than 49% of the voting shares or interest shares of legal entities conducting long-distance international communication using land

(cable, fibre-optic or radio-relay) connection cables (Law "On National Security of Republic of Kazakhstan", 6 January 2012). As a result, foreign-owned mobile operators had to rent Kazakhstan's lines for fixed broadband and intercity transmission services or set up joint ventures with smaller local intercity transmission operators. This contributed to the current limited share of foreign-owned operators on the fixed-line voice, data, and broadband internet markets. The maximum foreign equity limit in fixed-line telecommunications also contributed to the Kazakhstan's elevated score on the FDI Index in 2014.[25] FDI restrictions in the sector were also estimated to have an equivalent effect to a 15-20% *ad valorem* import tariff, significantly above the average import tariff level in Kazakhstan.[26]

However, as of January 2016, the amended legislation allows foreign ownership of legal entities operating or owning main fixed communication lines beyond the 49% equity threshold, except for the national operator JSC Kazakhtelecom,[27] provided that a special permit is delivered by the Ministry of Information and Communication jointly with the National Security Committee.[28] Despite this amendment, there is still room for improvement. The excessive market power of the incumbent state-owned operator in fixed line telephony and broadband internet services, combined with the absence of an independent regulatory authority in the telecommunication sector,[29] may have adverse consequences for the overall competitiveness of the economy. Reducing the remaining foreign investment restrictions concerning fixed-line international and inter-city telecommunication (including through the removal of the special screening procedure introduced in January 2016) could help increase competition and increase foreign direct investment in the sector. If the government decides to retain the procedure, it should ensure that the evaluation criteria and the administrative procedures used are clear and transparent, as highlighted in the OECD *Policy Framework for Investment*; and do not *de facto* limit market access in the sector. In 2012, the OECD recommended that Kazakhstan pursue its reform agenda in the telecommunication sector to open up to greater competition and create an independent regulatory authority for the sector (OECD, 2012).

Mass-media

As was the situation when the OECD released its first *Review* of Kazakhstan in 2012, the country retains legislated restrictions on foreign ownership in media: equity stakes in media companies are limited to 20% for foreign natural and legal persons.[30]

Security services

Foreigners, foreign legal entities and established foreign-controlled enterprises shall not provide security services or manage companies providing security services.[31]

Air transport

Until 2016, foreign investment in the air transport sector was allowed only up to 49% in companies involved in regular international and domestic flights for both passengers and cargo services. Since then, as of 1 January 2016, the equity restriction in air transport has been entirely lifted. At the time of writing, the authorities were nevertheless considering to reinstitute the previous restriction.

Measures notified by Kazakhstan under the National Treatment instrument for transparency purposes

Several policies applied by Kazakhstan qualify for notification as measures reported for transparency under the National Treatment instrument. These are listed in Annex B of this *Review*. Kazakhstan imposes conditions on key personnel both across economic sectors and in specific activities such as maritime and air transport and legal services. State and natural monopolies still apply in some significant sectors such as oil transport via trunk pipelines, transmission of electricity, ports and airports, and railways. In addition, foreign investment activities can be limited or banned in certain areas due to national security considerations.

Measures based on public order and essential security considerations

Measures based on public order and essential security interests must be reported for transparency purposes. Measures which do not openly discriminate between foreign-controlled enterprises and domestic enterprises but may result in difference in impact, imposing a greater burden on the foreign controlled-enterprise, are also notified for transparency purposes (OECD, 2005).

Cross-sectoral. Pursuant to the National Security Law (2012), foreign investment activities can be limited or banned in certain areas due to national security considerations. The Law takes a broad definition of national security by encompassing "public security' and "economic security", concepts that involve the protection of the "spiritual-moral values of Kazakhstan society"; "the integrity of society and its stability", the "favourable international situation of the state" and "economic development." The objective of economic security has been a justification for establishing a national security scrutiny or review in existing or subsequent laws, for example in the Law "On Subsurface and Subsurface Use", which has been amended in line with the National Security Law, which stipulates that "economic security" extends to the preservation and increase of the energy resources of Kazakhstan. Accordingly, the Government of Kazakhstan has the priority in purchasing the rights to subsurface utilisation, when sold by their current holder. Although not explicitly discriminatory, as

this provision applies equally to domestically-owned and foreign-owned juridical persons of Kazakhstan, it allows the government to prohibit companies with foreign participation from becoming a subsurface user. The decision on acquisition of alienable subsurface use right is taken by the competent authority on behalf of the Government of Kazakhstan.

Similar provisions apply to the sale/purchase of strategic objects, defined as a property of social and economic importance for sustainable development of Kazakhstan's society, the disposal of which will affect national security. Pursuant to Article 193-1 of the Civil Code and Article 188(3) of the Law on State Property, the sale/purchase of shares and any alienation of objects of strategic importance are subject to approval by the Government. Strategic assets may be in state ownership and in private ownership. The following assets may be considered as strategic objects: long distance railway networks; oil and gas transmission pipelines; national grid; refineries; some generation installations; nuclear energy facilities and other facilities indicated in Article 193-1 of the Civil Code. The list of objects of strategic importance is publicly available and regularly updated.[32] Although not explicitly discriminatory, these provisions allow the authorities to bar the acquisition by foreigners of strategic objects, including the participation of foreign investors in the privatisation of certain assets deemed to be strategic.

While it is legitimate for countries to protect their essential security interests, it is important that such policies are based on the principles of proportionality, transparency, predictability and accountability as recommended in the OECD 2009 Guidelines. To ensure predictability and accountability, the review or authorisation procedures should be based on clear criteria and specify the modalities, including the documents to be submitted by applicants, the timeframe for conducting the review of a transaction, and the possible appeal or redress procedures against the security- and strategic sectors-related investment policy decision (Wehrlé and Pohl, 2016). As already recommended by the OECD in its 2012 *Review* of Kazakhstan, such measures would help reduce the current legal and regulatory uncertainty in Kazakhstan's policies based on national security considerations (OECD, 2012).

Agricultural land in border areas. Agricultural land immediately adjacent (3-km zone) to the protected zone of the state border of the Republic of Kazakhstan can only be leased by citizens and legal entities of Kazakhstan. Foreigners and foreign legal entities are prohibited to lease or acquire agricultural land in this zone.[33] Pursuant to paragraph 28 of Article 2 of Law "On the State Border of the Republic of Kazakhstan", a border zone is a part of the territory of the Republic of Kazakhstan adjacent to the borderland within the territory of administrative districts.[34] The minimum distance from the border that is prohibited for lease or purchase by foreigners is within the

territory of 27 km and/or within administrative territories (districts) adjacent to Kazakhstan's state border and banks of the border rivers, lakes and other basins. On the coast of the Caspian Sea, the distance is within the 25 km adjacent to the shoreline of the Caspian Sea.[35]

Other measures reported for transparency

Kazakhstan also imposes certain conditions on corporate organisation as well as limits on key personnel and other foreign staff both across sectors and in specific sectors (maritime and air transport, legal and para-legal services, forensic accounting, property management and tourism).

Corporate organisation. Kazakhstan's legal framework contains few corporate organisations requirements and, with some exceptions, they are applied on a non-discriminatory basis to foreign and domestic investors. For example, airlines performing regular flights must be joint-stock companies and this incorporation requirement applies to both domestic and foreign investors.[36] Exceptions include the prohibition for foreigners to establish as individual entrepreneurs.[37] A foreign company must also establish a subsidiary (not a branch) to perform maritime transport and financial services (bank, insurance and brokerage services) in Kazakhstan.

Maritime transport

Under the Shipping Law, only ships and vessels with Kazakh state flag or the flag of a Caspian sea country, established as a local subsidiary and registered in Kazakhstan are allowed to provide maritime cabotage services, subject to administrative authorisation by the government.[38] Foreign legal entities operating in the Caspian Sea according to production sharing agreements (e.g. contracting companies, operators, agents) may also fly the national flag.[39] Thus, the right to fly under the state flag of the Republic of Kazakhstan is given to ships operating in the property of juridical persons, established in Kazakhstan, except for foreign legal entities operating in the Caspian Sea under the Production Sharing Agreements.

Financial services

Banks and insurance

Since 2005, the sector has been almost completely opened to foreign investment. The principal requirement remaining for foreign investors in the banking sector concerns branching, which is not a restriction in the meaning of the *National Treatment* instrument. Foreign banks may open a representative office but may not open branch offices. The insurance sector is governed by the 2000 Law on Insurance Activities, as amended. As in banking, non-resident

insurance companies may open representative offices but are prohibited from establishing branches. This requirement will however soon be phased out in accordance with the Schedule of Specific Commitments of Kazakhstan under the GATS: starting from 16 December 2020, non-resident banks, insurance (reinsurance) companies, companies providing brokerage services will be allowed to open a branch in Kazakhstan, subject to the terms and conditions established by Kazakhstan's legislation.[40]

Generally, resident and non-resident legal entities (as well as individuals) may act as founders, or be shareholders of local insurance companies or banks. However, entities registered in certain offshore jurisdictions[41] as defined by a Resolution of Kazakhstan's agency for financial market regulation, or their individual shareholders, cannot be founders or shareholders of a local bank or insurance company.[42], This limitation does not apply to insurance (reinsurance) companies or banks that are subsidiaries of insurance companies or banks that have a minimal international credit rating of BBB or equivalent (foreign currency rating, international scale).[43]

Other financial services

Securities dealing and stock brokerage services have been gradually opened to foreign investment. As a rule, foreign firms can set up and be shareholders of companies providing specialised services on financial markets (securities dealing, stock brokerage services, underwriting new issues) and of investment funds, provided they are not controlled by legal entities registered in offshore jurisdictions (as listed in the Resolution No. 385 of the National Bank of Kazakhstan dated 24 December 2012). This restriction does not apply to companies that are subsidiaries of non-resident companies that have a minimum long-term credit rating of BBB on foreign currency (as rated by international ratings agencies listed in the Government Resolution No. 385).[44]

With regards to pension funds, the new Law on pension provision (No. 105-V) adopted on 21 June 2013, as amended, provides that asset management services for pension funds can be provided by companies whose shareholders are residents and resident legal entities. There is no discriminatory provision regarding foreign-owned established enterprises. Non-resident asset management companies can also offer those services if they respect minimal financial rating criteria and are not controlled by entities from offshore jurisdictions.

Key personnel. As noted earlier in this Chapter, Kazakhstan's legal framework contains a number of specific rules for employing foreign workers and restrictions concerning the share of foreign staff apply to almost each type of position.[45] With a few exceptions (e.g. heads of representative offices or branches of foreign legal entities and Armenian, Belarus, Kyrgyz and

Russian citizens), limits on employment of foreign staff apply to each employee category:

- The number of citizens of Kazakhstan in first (executives and their deputies) and second (managers and specialists) categories shall be not less than 70% of the staff;
- The number of citizens of Kazakhstan in third (technical experts) and fourth (qualified workers) categories shall be not less than 90% of the staff;
- The number of foreign transferees (i.e. foreigners transferred in a Kazakh affiliate of their employer) shall be not more than 50% of the relevant staff category in each company.

In addition, in accordance with sector-specific laws, certain professional activities can only be performed by citizens of Kazakhstan. Thus in maritime transport, foreign persons cannot take the position of the captain, chief captain's mate, chief engineer and signaller of a ship.[46] In the air transport sector, only a citizen of the Republic of Kazakhstan may be the head of the aviation security service of airport or of an air company providing scheduled air transport services, or can be the air security officer of an operator providing non-scheduled air services and aerial works.[47] In the field of legal or para-legal services, similar restrictions apply: only a citizen of Kazakhstan may be an advocate or notary, or a candidate advocate/notary (intern); a public and private bailiff; and a patent attorney.[48] Restrictions also apply to the forensic profession, the management of property in bankruptcy procedures, and the tourism industry.[49]

Government purchasing. Public procurement represents an important share of Kazakhstan's economy. In 2010, the aggregate value of public procurement amounted to 6.6% of the country's GDP and government purchasing amounted to 43% of total governmental expenses (United Nations Economic and Social Commission for Asia and the Pacific, 2014). Kazakhstan's legislation allows locally established foreign-controlled enterprises to engage in government procurement on the same basis as domestic firms with no foreign equity.[50] With regards to non-resident foreign enterprises, the new 2015 Public Procurement Law has kept the concept, introduced in 2014, of "national regime" according to which public procurement is open to foreign and domestic economic operators on equal grounds, provided that the requirement to grant such a regime is set by the international treaties ratified by the Republic of Kazakhstan and pursuant to the terms and conditions set forth in such treaties.[51] As at 31 December 2016, Kazakhstan provided on a reciprocity basis national treatment for the purposes of participation in public procurements only for the Member-States of the Eurasian Economic Union (Armenia, Belarus, Kyrgyzstan and Russia) under the Treaty on Eurasian Economic Union of 29 May 2014.

Sectors subject to public/private/mixed monopolies or concessions. Monopolies and concessions are notified under the *National Treatment* instrument for transparency purposes as well. Monopolies can take two forms in Kazakhstan: i) a public monopoly, run by the state or managed by local governments ("state monopolies"); and ii) natural monopolies. There are no private monopolies in Kazakhstan, and the term "private monopoly" is not provided for in Kazakhstan's legislation.

Public monopolies

The Kazakh legislation defines a state monopoly as an activity in which competition would be detrimental for "the constitutional order, national security, public order, human rights and freedoms, and public health".[52] There are currently about 20 state monopolies in Kazakhstan active in some 25 economic sectors (See Annex B). They are not registered or classified systematically, as state monopolies are created and regulated by specific legislation in the sectors in which they are established (OECD, 2016b). Most of the existing state monopolies are operating in areas which traditionally were considered basic public services such as medical equipment control, production of passports, or assessment of patent applications. Some state monopolies are also granted in sectors where the risks of competition for the environment, such as wild life protection, are considered to be too high by the Kazakh authorities.

Natural monopolies

A vast range of important industries and economic sectors are natural monopolies in Kazakhstan. The importance of natural monopolies in Kazakhstan can be seen by the fact that some of the country's largest and most powerful corporations, such as the Kazakhstan Electricity Grid Operating Company (KEGOC) (national transmission grid operator), KazTransOil (national oil transporter in Kazakhstan accounting to 65% of all oil transported in the country), KazTransGas (the state corporation responsible for 95% of natural gas transportation via gas pipelines) and the National Company Kazakhstan Temir Zholy (the national railway company of Kazakhstan) are subject to natural monopoly regulation.

The Law on Natural Monopolies and Regulated Markets of 1998, as amended, forms the legal framework. It defines a natural monopoly as a state of the market that does not allow for competition in the production of certain goods or the provision of certain services because it is either impossible or economically inefficient in the area.[53] The law contains an exhaustive list of industries which are recognised as 'natural monopolies'. In total, some 15 economic sectors or business activities are currently subject to public monopoly in Kazakhstan.[54] They include:

1. transportation of oil, oil derivatives via trunk pipelines;
2. storing and transporting natural gas via trunk and/or distribution pipelines, operation of natural gas pipelines, usage of natural gas distribution systems;
3. transportation and/or distribution of electrical energy;
4. thermal generation, transmission, distribution and/or supply;
5. provision of electricity dispatch services;
6. services relating to organizing of balancing generation and consumption of electrical energy;
7. operation of main-line railways;
8. provision of railway services under concession agreements in the absence of alternative railway track;
9. operation of branch railway lines;
10. air navigation;
11. airport and harbour services;
12. provision of telecommunication services, if there is no other competing telecom operator due to technical impossibility, or economical unfeasibility, except for universal telecommunication services;
13. universal postal services;
14. leasing to other entities of duct banks and equipment for connecting telecommunication lines to terrestrial telecommunication network (of incumbent telecom operator);
15. operation of water and sewage systems.

All in all, the state register of enterprises acting in these naturally monopolistic spheres includes 1 186 economic entities. At the end of 2015, these enterprises provided 1 643 regulated services to consumers, including: 850 in water supply and utilisation; 456 in electric and heat energy sector; 279 in the transport area; 52 in oil and gas transportation; and 6 in post and telecommunications sector (OECD, 2016b).

In 2014, the government declared its intention to introduce competition into potentially competitive areas of the natural monopoly sectors and its readiness to improve the investment climate and to attract private investments (including through PPPs) into the housing and utilities sector, as well as other industries subject to natural monopoly regulation. In this context, it adopted a roadmap for an analysis of the regulated sectors to facilitate their transition from a state of natural monopoly to a competitive status. This roadmap defined eight markets where this analysis had to be conducted by the relevant authorities in 2014-15. These sectors included services in the areas of railroads, sea ports, telecommunications and oil transport. As a result of these initiatives,

the government approved in December 2015 an ambitious privatisation programme which targets some enterprises acting in these naturally monopolistic spheres (see below, on privatisation).

Concessions

The July 2006 Concession Law No. 167-III, as amended (the "Concession Law"), is the principal source of rules governing concessions. In addition, general laws such as the Civil Code and the new Entrepreneurial Code, sector specific laws[55] as well as sub-laws are applicable to concessions.[56]

The majority of current concessions in Kazakhstan are in the energy sector (exploration and exploitation of oil and gas), in social infrastructure and the transport sector (road, railroad and airport). In principle, infrastructure facilities in all economic sectors can be subject to a concession agreement, with a few exceptions, such as trunk rail networks, navigable waterways, lighthouses and other navigation devices and signs, and water structures.[57] Such concession agreements are open to foreign investors.[58] Although a number of concession agreements have been implemented, none of them have been completed. As a result, it is still too early to judge their success. International institutions such as the EBRD and the UNECE have seen Kazakhstan's Concession Law and its subsequent amendments as a basic piece of legislation enabling the implementation of concessions in infrastructure based on rather good practices and a competitive selection (EBRD, 2014; UNECE, 2013). The World Bank has nevertheless noted that substantial legal barriers remain due to excessive regulation and lack of clarity in implementation arrangements.[59] Against this background, it is expected that the Law on Public Private Partnerships (PPPs), enacted at the end of 2015, will enhance the enabling environment to attract private sector investment in infrastructure through PPPs. The regulatory framework and recent developments of PPPs in Kazakhstan is detailed further in Chapter 5 on investment promotion and facilitation.

Enhancing competiveness

Privatisation process

State-owned enterprises (SOEs) still represent a large part of the economy in Kazakhstan. In spite of the rapid privatisation of businesses in the 1990s and 2000s,[60] the state has secured control over the most important economic sectors like oil and gas production, electricity, transport and telecoms.[61] These sectors are dominated by the few national holding companies established and managed by the government.[62] At the end of 2015, public and state-owned companies still accounted for about 35%-40% of GDP according to some estimates (OECD, 2016c), totalling more than 7 000 companies.[63] As seen above, in some

sectors such as infrastructure, the state is either the sole provider or plays a dominant role through its control of the largest incumbent operator.

The Civil Code No. 409-I from 1 July 1999 (last amended on 27 April 2015); the Law No. 413-IV "On State Property" dated 1 March 2011; the Law No. 434-V "On Public Procurement" dated 4 December 2015; and the government Decision No. 920 of 9 August 2011 "On Approval of the Rules of the Sale of Privatization Objects", as amended on 31 December 2015, are the main legal acts regulating privatisations in Kazakhstan. State property can be sold to individuals, domestic (non-state) legal entities and foreign legal entities. There are no restrictions for foreign participation in privatisation.

In December 2015, the government approved a new wave of privatisation for 2016-20 aimed at privatising 783 state owned companies and subsidiaries of national holdings.[64] Such privatisation has been one of the main response measures of the government intended to reduce the presence of the state in the national economy and cut down subsidies to businesses as well as make up for the budget loss from the lower oil price.

Assets in the atomic energy, oil and gas and mining sectors will be sold. Kazakhstan's largest state-owned companies such as Kazatomprom nuclear company, Samruk-Energy company, Tau-Ken Samruk mining company and KazMunaiGaz (oil and gas company) are planned to be transferred to the private sector through initial public offering (IPO). Among KazMunaiGas's subsidiaries, the Atyrau refinery, Pavlodar Petrochemical Plant, PetroKazakhstan Oil Products (Shymkent refinery), Kazmortransflot National Maritime Shipping Company and others are also planned to be transferred to the private sector. Companies operating in the telecommunication and postal services sectors such as "Kazakhtelecom", "Kazpost", and "Trancetelecom" will also be sold. The National Company Kazakhstan Temir Zholy (the national railway company of Kazakhstan) is also planned to be transferred to the private sector through initial IPO.[65] Tenders and auctions will be opened to both local and foreign investors.[66] The target indicators are: i) reduction of quasi-state companies owned by the central government to 15% by 2021 and ii) transfer of 5% of companies owned by the local governments to the private sector.[67] Taking into account the plans for broadening the ownership of state enterprises through initial public offering, the state and SOEs should take steps to ensure that all shareholders are treated fairly, which also means that the state should behave as an informed and professional shareholder, avoid ad-hoc intervention in the operation of SOEs and act only through the shareholder rights in concert with the boards of directors.

Given the strong role of SOEs in Kazakhstan's economy, the OECD in 2012 called for the strengthening of corporate governance in SOEs (OECD, 2012). Since then, all SOEs are required by law to publish annual reports and to go

through an independent auditing process.[68] In parallel, the authorities have made continuous efforts to reform the accounting legislation and align standards applicable in Kazakhstan with international accounting standards. Despite these reforms, audits of SOEs have proved to be ineffective[69] and there is still a long way to go to improve accountability and transparency in these companies. While the Kazakh authorities continue to undertake reforms aimed at attracting foreign investment further, they should also identify new ways to ensure that all corporate governance standards applicable to private companies also apply to SOEs. There should also be a clear separation between the state's ownership function and other state functions that may influence the conditions for state-owned enterprises, particularly with regard to market regulation. The OECD *Guidelines on Corporate Governance of State-Owned Enterprises* contain a wealth of practical experience, which is highly pertinent to the on-going reform priorities in Kazakhstan (OECD, 2015).

Samruk-Kazyna is an example of promising developments as it has recently taken steps to improve its corporate governance framework. A new Corporate Governance Code was adopted in 2015 and applies to all organisations in which Samruk-Kazyna directly or indirectly owns more than 50% of voting rights. The Code makes clear role of the Government as ultimate shareholder, describes specifics of Samruk-Kazyna in relation to its portfolio, emphasizes the role of the Board of directors and Risk management, Sustainable development is addressed; the Code calls for transparency and accountability, observance of human rights, prevention of environmental abuse, corruption prevention and other integrity related aspects. It also requires disclosure of these issues in the annual reports of the Fund and its subsidiaries (See also Chapter 7). Another promising development relates to the Government's efforts aimed at better aligning the Model Code of Corporate Governance of Joint Stock Companies with State Participation of 2007 with the principles and recommendations contained in the OECD *Guidelines*.[70]

Competition policy

Given that SOEs still represent a large part of the economy in Kazakhstan, an effective competition authority is an essential precondition for a more level playing field for private investor in Kazakhstan. At the core of this role is the need for sufficient human and material resources.

As already noted in the previous *Investment Policy Review* of Kazakhstan, the country has made perceptible progress in establishing a basic legal and institutional framework for competition policy over the past decade. In particular, Kazakhstan's competition authority, the Agency on Protection of Competition, has become increasingly active, notably in encouraging demonopolisation and the reduction of state interference in the economy. Concerns were nevertheless expressed in the *Review* that the authority did not

appear to dispose sufficient human and material resources to carry out its growing responsibilities in addition to its main mission to facilitate fair competition and prevent and investigate violations of anti-monopoly legislation (OECD, 2012a).

Since then, Kazakhstan has undertaken a series of reforms in the field of competition. In particular, important changes were made in 2014, with the establishment of the Committee on Regulation of Natural Monopolies and Protection of Competition (KREMZK) as the new competition authority.[71] As a result of this move, KREMZK counted over 500 employees at the end of 2015. Prior to this, in 2013, 200 people were working in the Agency on Protection of Competition. The agency's budget also nearly tripled between 2012 and 2014, from USD 4.5 million to USD 11.7 million. These figures could be seen as illustrating the willingness on the part of the Kazakh government to strengthen the role of the authority as a governing body in the sphere of competition responsible for both enforcement and policy.[72] They are nevertheless primarily the result of the merger of two previous agencies, the former Agency on Protection of Competition and the former Agency on Regulation of Natural Monopolies, previously responsible for regulating natural monopolies. It would appear that the merger has created more opportunities for the economic regulator rather than for the competition authority (OECD, 2016b).

KREMZK is also not an independent authority, as it is housed in the Ministry of National Economy. One could argue that the merits of the agency lie in being housed in the government, as this structural setting places the authority close to process to draft laws and regulations, since the Ministry is also mandated to set policy priorities for competition. Nevertheless, there is a possible downside of Kazakhstan's choice to locate its competition authority in the Ministry of National Economy. In its 2016 peer review of Kazakhstan's competition law and policy, the OECD noted that the competition authority's positioning within the structure of the executive power in Kazakhstan's highly centralised government might have a direct impact on the agency's ability to influence state policy and implement its law enforcement activity. The OECD further noted that this positioning was in contrast to the role of independent law enforcer as suggested by President Nazarbayev in his 2015 Plan for the Nation in which he called for the alignment of Kazakhstan's competition law and enforcement with the OECD standards (OECD, 2016b).

Since this structural setting was introduced recently, as of the time of this *Review* there was not yet sufficient practice to make a conclusive argument as to whether the agency, in its current form, has become more effective. In 2015, Kazakhstan was still placed relatively low in terms of its competition policy in the World Bank's *Global Competitiveness Report* 2014-2015. Kazakhstan ranked 111st out of 144 countries regarding the intensity of local competition and 94th in terms of effectiveness of its anti-monopoly policy. Legislative and

institutional changes aimed at improving the competition climate are nevertheless expected to take place in the near future as the result of Kazakhstan's decision in 2014 to join the Eurasian Economic Union (EAEU).

The development of Kazakhstan's competition law and policy could benefit substantially from EAEU membership, as it requires the establishment among Member States of a solid legal and institutional framework for competition. According to the OECD, "a substantive implementation of the EAEU Model Law could give a serious impetus to the development of Kazakh competition policy in the direction of recommended OECD standards" (OECD, 2016b). At the end of 2015, Kazakhstan already included some provisions of the EAEU model law in its Entrepreneurial Code, which entered into force on 1 January 2016 and incorporates and supersedes the law "On Competition" adopted in 2008. Changes in the field of antimonopoly regulation are related to several issues including: opportunity is now provided for preliminary reviews of the market entities' agreement by the antimonopoly authority; the Anti-Monopoly Agency may now issue a "notice" without investigation if it finds out that a certain market entity abuses its dominant or monopolistic position; starting from 1 January 2017, a company under antitrust investigation will be able to initiate a review of a draft report on antitrust compliance findings by a conciliatory commission involving independent experts. At the end of 2016, a draft law aimed at addressing the recommendations of the OECD, including reportedly the strengthening of the new competition authority's independence, was being discussed in parliament.

Kazakhstan in the OECD FDI Restrictiveness Index

The above description of reform processes for key sectors of Kazakhstan's economy cannot fully capture the country's enabling environment for investment. Quantitative indicators have in this regard proven highly effective in drawing attention to the burdens of statutory restrictions on FDI, identifying priorities for reform and communicating success and progress. Kazakhstan's FDI regulatory restrictiveness is assessed against a group of 69 economies, including all OECD and G20 economies. The *FDI Regulatory Restrictiveness Index* (FDI Index), developed by the OECD, seeks to gauge the restrictiveness of a country's FDI rules in 22 sectors taking into account four types of measures: equity restrictions, screening and approval requirements, restrictions on key personnel, and other operational restrictions such as for instance restrictions on branching (see Box 2.3). The FDI Index constitutes one component of indicators used for the OECD's *Going for Growth* policy recommendations. It is also used on a stand-alone basis to assess the restrictiveness of FDI policies in reviews of candidates for OECD accession and in the OECD *Investment Policy Reviews* series. It is also an important component of any review of candidate Adherents to the *Declaration on International Investment and Multinational Enterprises*.

The FDI Index does not provide a full measure of a country's investment climate as it does not score the actual implementation of statutory restrictions and does not take into account other aspects of the investment regulatory framework, such as the nature of corporate governance, the extent of state ownership, and institutional and informal restrictions which may also impinge on the FDI climate. Nonetheless, FDI rules are a critical determinant of a country's attractiveness to foreign investors and the FDI index, used in combination with other indicators measuring various aspects of the FDI climate, contributes to assess countries' international investment policies and explain variations among countries in attracting FDI.

Box 2.3. **Calculating the OECD FDI Regulatory Restrictiveness Index**

The OECD FDI Restrictiveness Index covers 22 sectors, including agriculture, mining, electricity, manufacturing and main services (transports, construction, distribution, communications, real estate, financial and professional services).

For each sector, the scoring is based on the following elements:

- The level of foreign equity ownership permitted;
- The screening and approval procedures applied to inward foreign direct investment;
- Restrictions on key foreign personnel; and
- Other restrictions such as on land ownership, corporate organisation (e.g. branching).

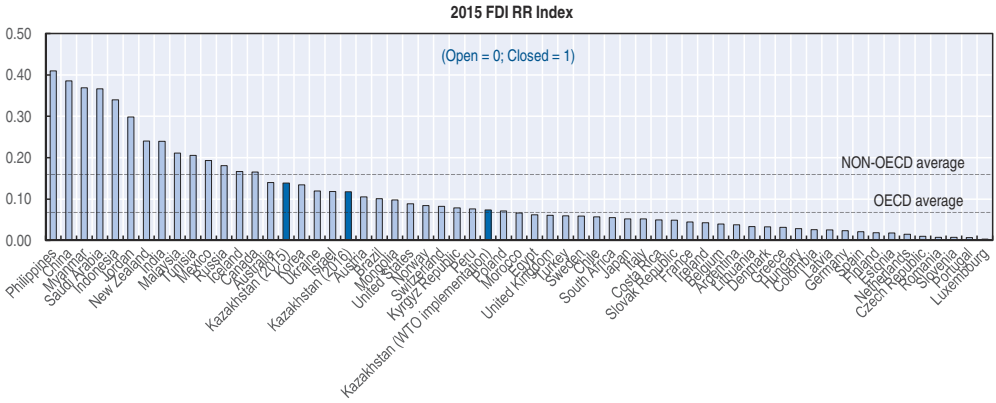
Restrictions are evaluated on a 0 to 1 scale: "0" corresponds to the absence of restrictions and "1" indicates a sector totally closed to FDI. The overall restrictiveness index is the weighted average of individual sectoral indexes.

The measures taken into account by the index are limited to statutory regulatory restrictions on FDI (as reflected in the countries' lists of exceptions to the *National Treatment* instrument and measures notified for transparency) without assessing their actual enforcement. The discriminatory nature of measures, i.e. when they apply to foreign investors only, is the central criterion for scoring a measure. State ownership and state monopolies to the extent they are not discriminatory towards foreigners are not scored. Incorporation requirements, as they restrict FDI in the form of branching, are also taken into account although they are not covered and, thereby, listed as an exception in the *National Treatment* instrument.

For the latest scores, see *www.oecd.org/investment/fdiindex.htm*. For an explanation of the methodology, see OECD Working Paper on International Investment No. 2010/3 *OECD's FDI Restrictiveness Index: 2010 Update* available at *www.oecd.org/daf/inv/investment-policy/WP-2010_3.pdf*.

As of December 2015, Kazakhstan already maintained a relatively open statutory regime for foreign investors, despite still above OECD average levels (Figure 2.2). A few service sectors remained partly off limits to foreign investors, notably media, air transport, banking and insurance and fixed telecommunications. Foreign investors in primary sectors too faced discriminatory restrictions relating to the use of agricultural and forestry land. Kazakhstan also maintained somewhat burdensome conditions with regards to the employment of key foreign personnel, which apply horizontally across economic sectors, and are relatively less typical among other Adherents.

Figure 2.2. **FDI Regulatory Restrictiveness score by country**



Note: Data as of December 2015, with the exception of Kazakhstan simulated results.
Source: OECD FDI Regulatory Restrictiveness (*www.oecd.org/investment/fdiindex.htm*).

StatLink http://dx.doi.org/10.1787/888933452820

Nevertheless, Kazakhstan has made strides in committing to important reforms during its WTO accession process, which will likely bring its statutory regime to foreign investors much closer to the OECD average (see Figure 6.2 in Chapter 6). The government has already anticipated the need to implement some of these reforms, notably lifting, as of January 2016, the previous foreign equity restriction in fixed-line telecommunications. Though no WTO commitment exists, it lifted, as noted earlier in this Chapter, the equity restriction in air transport. Such reforms, together with other changes expected to be implemented within five years of Kazakhstan's accession to WTO, will support an even more open environment for foreign investors and contribute to greater productivity (see trade section in Chapter 6 for more detail). Liberalisation may be provided for under investment treaties as well (see Box 2.4 below, as well as next chapter on investment treaties).

Box 2.4. **Investment treaties as a tool to liberalise investment policy**

Increasingly, international treaties (IIAs) are being used to liberalise investment policy. These provisions are often referred to as applying to the "pre-establishment" phase of an investment. A key tool to foster liberalisation is to extend the national treatment (NT) and most-favoured nation (MFN) standards to those covered foreign nationals seeking to make investments. The Kazakh agreement with Japan grants covered investors NT and MFN, but only extends MFN to the pre-establishment phase.[73] When countries grant national and/or most-favoured nation treatment, whether pre- or post-establishment, they typically do so subject to reservations. There are two broadly different approaches:

1. A negative list-approach typically provides that MFN and NT are generally afforded, except for specific exceptions or provisions ("negative lists") specified in annexes;
2. A positive-list approach specifies that its liberalisation provisions only apply to specific identified sectors.

The Kazakhstan-Japan IIA does not contain any annexes setting out the exceptions, but provides for certain cross-sectoral exceptions for MFN and specifies that MFN does not apply to matters related to the acquisition of land property (art. 4[2]).

Compared to other economies and the provisions of recent investment treaties, such as the Trans-Pacific Partnership agreement, CETA, and agreements in ASEAN, Kazakhstan makes little use of investment treaties as a tool to foster investment liberalisation. Kazakhstan might wish to consider whether such investment liberalisation provisions could be a useful complement to its other efforts to attract and facilitate new investments.

Policy recommendations

The authorities have made strides in opening the country to international investment. Nevertheless, given the statutory restrictions that still apply in sectors such as mass-media and telecoms – areas where most OECD countries do not find it necessary to maintain restrictions –, Kazakhstan's score in the OECD FDI Regulatory Restrictiveness Index is higher than the average of OECD countries, albeit lower than the non-OECD countries average. Kazakhstan has committed to important reforms during its WTO accession process, which should bring its statutory regime to foreign investors much closer to the OECD average in the coming years. Such reforms, like in financial services where operations of branches of foreign-owned banks will be allowed by 2020, should support a more open and transparent environment.

- *Consider further liberalization in sectors that remain relatively closed* to foreign investment and where WTO market access commitments have been limited, such as ownership of land.
- *Ensure that administrative procedures*, including screening mechanisms, *do not limit market access* in practice in sectors where market access has recently been deepened, such as telecommunications.
- *Restrain on the application of exceptions based on essential security interest* listed under the National Treatment instrument list of exceptions, including adoption of best practices concerning investment policies relating to national security, taking into account the principles of non-discrimination, proportionality, transparency and accountability as enshrined in the OECD *Guidelines for Recipient Country Investment Policies Relating to National Security*.
- *Pursue further efforts aimed at simplifying administrative procedures for hiring foreign key personnel* to facilitate access of local firms to talent worldwide. Local content requirements that apply to labour are being reduced but, together with other administrative procedures, still remain a barrier. Administrative capacity of institutions dealing with issuing relevant permits could also be strengthened to reduce delays while retaining appropriate control.
- *Keep strengthening the competition law regime*, notably in the areas highlighted in the OECD's 2016 peer review of Kazakhstan's competition law and policy, such as improving the independent action of the new competition authority.
- *Pursue efforts aimed at supporting* the development and enforcement of *corporate governance frameworks for state-owned enterprises (SOEs)*.

Notes

1. Until 2017, the yearly quota for foreign labour was set annually by the government on the basis of the needs of each local (regional) authority. The local needs were based on an assessment of local labour market and of employer's applications submitted to the Ministry of Healthcare and Social Development in which they specified their needs in terms of labour force. The Ministry then developed the draft of the government resolution establishing the annual quota. The Government amended these rules in 2016, with entry into force in January 2017. According to the new rules, the annual quota for foreign labour recruitment is now determined on the basis of industries' needs. Source: official website of the Prime Minister of Kazakhstan: "Kazakhstan to distribute quotas for foreign workers by economic sectors", 28 October 2016.
2. Government Resolution No. 45 of 13 January 2012 on "Quota establishing regulation for foreign labour force in Kazakhstan, terms and conditions for issuing permits to foreign workers for employment and to employers for engaging foreign labour force". In 2016, the Resolution contained a total of 17 exceptions.

3. Ibid.
4. Statistics provided by the Government of Kazakhstan.
5. Berry Appleman & Leiden LLP, "Kazakhstan – New rules set for regional work permits, hiring foreign managers"(2 September 2015).
6. Law No. 365-V "On Amendments and Addenda to Certain Legislative Acts of the Republic of Kazakhstan in Connection with Joining the World Trade Organisation" of 27 October 2015, which entered into force on 9 November 2015. Regulations in this sphere were laid down in the Government Decree No. 173 of 31 March 2016 ""On Introduction of Amendments into the Decree No. 45 of the Government of the Republic of Kazakhstan of 13 January 2012 on Approval of the Rules for Establishing Quota for Foreign Labour Engagement in the Republic of Kazakhstan, Rules and Conditions for Issuing Job Placement Permits to Foreign Employees and Work Permits to Employers for Foreign Labour Engagement, and on Introduction of Amendment into the Decree No. 836 of the Government of the Republic of Kazakhstan of 19 June 2001 on Measures for Implementation of the Law of the Republic of Kazakhstan of 23 January 2013 on Population Employment, and Decree No. 673 of the Government of the Republic of Kazakhstan of 2 July 2013 on Approval of the Rules for Privatization of Dwellings from the State Housing Fund".
7. Law No. 482-V "On Employment" dated 6 April 2016, which entered into force on 18 April 2016.
8. Pursuant to Law No. 482-V, the requirement to search for suitable workers on local labour market before attracting foreign ones will be eliminated upon expiration of a 5-year period after Kazakhstan's accession to the WTO (i.e. by November 2020).
9. Work permits are delivered by regional authorities at the oblast level. Pursuant to the amendments introduced by the Decree of the Government No. 844 dated 28 October 2015, work permits cannot be issued for two or more administrative regions.
10. Decree No. 173 of the Government dated 31 March 2016.
11. Decree No. 190 of the Government dated 7 April 2016 "On Introduction of Amendments to the Decree No. 148 of the Government of the Republic of Kazakhstan of 21 January 2012 on Approval of the Rules for Immigrants' Entry and Stay in the Republic of Kazakhstan, and Their Exit from the Republic of Kazakhstan, and the Rules for Migration Control and Recording of Foreign Citizens and Stateless Persons Illegally Crossing the State Border of the Republic of Kazakhstan, Illegally Staying in the Territory of the Republic of Kazakhstan, and Persons Prohibited to Enter the Territory of the Republic of Kazakhstan".
12. Paragraph 4(11) of the Government Resolution No. 45 of 13 January 2012, last amended on 31 March 2016.
13. Slightly different rules apply to intra-corporate transfers: the employer is required to notify the local authorities within ten calendar days of the foreign worker's entry into the territory of Kazakhstan.
14. Law No. 365-V "On Amendments and Addenda to Certain Legislative Acts of the Republic of Kazakhstan in Connection with Joining the World Trade Organisation" of 27 October 2015, which entered into force on 9 November 2015.
15. Article 76.9 of the Law of the Republic of Kazakhstan No. 291-IV "On Subsurface and Subsurface Use" of 24 June 2010 prior to its amendment.

16. Inconsistent measures contained in investment contracts concluded prior to January 2015 will cease to be enforced as of the date of expiration of the initial duration of the contracts or by 1 January 2021, whichever takes place sooner.

17. The local content in personnel is established in accordance with the Law on Employment of the Population dated 23 January 2001, as amended. As noted above, the legislation of Kazakhstan distinguishes work permits depending on the category of workers, establishing different conditions of validity, extension, etc.

18. Under Kazakhstan's legislation, as amended by Law No. 365-V of 27 October 2015, "Kazakhstan manufacturers and producers of works and services" are defined as individual entrepreneurs and legal entities organised under Kazakhstan's laws and located on its territory, were at least 95% of all employees are citizens of Kazakhstan without regard to the numbers of managers and specialists carrying out labour activities in Kazakhstan within the framework of intra-corporate transfers. The number of such managers and specialists is nevertheless not to exceed 25%, and - starting from 1 January 2022 - 50% of the total number of employees in each respective category.

19. Paragraph 2 of Article 47 of the Law "On Subsurface and Subsurface Use", which provides for a maximum of 50% of local content requirement in services and works.

20. In the President's national development Strategy 2050 articulated in December 2012, the agro-food sector is identified as one of the eight priority sectors for diversification.

21. Article 23, 24 and 37 of the Land Code dated 20 June 2003, as amended.

22. Presidential Decree No. 248 of 6 May 2016 imposing moratorium on certain norms of the land legislation and Law of the Republic of Kazakhstan "On suspension of certain provisions of the Land Code of the Republic of Kazakhstan and enactment of the Law of the Republic of Kazakhstan as of 2 November 2015 "On amendments to the Land Code of the Republic of Kazakhstan" adopted in June 2016. Protesters were concerned that amendments to the land law increasing lease terms for foreigners for renting agricultural land from 10 to 25 years would be to the detriment of Kazakh citizens and landowners (see Chapter 7).

23. The two largest operators by far are foreign-owned Kcell (13.1 million subscriptions at the end of 2014) and KaR-Tel (Vimpelcom group, 9.8 million subscriptions). Source: Vimpelcom 2014 *Annual report* p.70.

24. Source: Kcell annual report, p. 8.

25. According to the OECD FDI Restrictiveness Index, fixed telecommunications was the most protected sector in Kazakhstan with a score of 0.8 (on the scale from 0 to 1), nearly eight times higher than the OECD average and five times higher than the average score of Kazakhstan in all sectors (0.2).

26. Jensen and Tarr (2007) estimate that the barriers to FDI in fixed-line and mobile telecommunications in Kazakhstan amounted to 20 and 15% ad valorem tariff equivalent, respectively.

27. In case of JSC Kazakhtelecom, and its possible successors, the 49% total foreign equity limitation in the charter capital (stocks or shares) will be maintained. Source: Kazakhstan's WTO Services Schedule.

28. Article 23 of the Law "On National Security" No. 527-IV of 6 January 2012, as amended.

29. The Communication, informatization and information Committee (CIIC), which is the main government body in charge of regulating the telecommunication sector

since October 2014, is not an independent authority, as it is a unit within the Ministry for Investments and Development.

30. Article 23 of the Law "On National Security" No. 527-IV of 6 January 2012, as amended.

31. Article 5 of Law "On Security Services" No. 85 of 19 October 2000.

32. The list is publicly available on the official websites of the Ministry of National Economy (www.minplan.kz) and the Ministry of Justice (www.minjust.kz) in both Kazakh and Russian.

33. Articles 23 and 24, Land Code dated 20 June 2003 No. 442, as amended.

34. Law No. 70-V "On the State Border of the Republic of Kazakhstan" of 16 January 2013.

35. Government Resolution of the Republic of Kazakhstan No. 365 "On Establishment of the Limits of Borderland, Quarantine Zone and Border Zone" of 16 April 2014.

36. Law No. 339-IV "Concerning the Use of Air Space of the Republic of Kazakhstan and Civil Aviation" of 15 July 2010.

37. Only a citizen of the Republic of Kazakhstan can be an individual entrepreneur: Entrepreneurial Code of the Republic of Kazakhstan No. 375-V of 29 October 2015.

38. Law of the Republic of Kazakhstan No. 284-II "On Merchant Shipping" of 17 January 2002 and Law of the Republic of Kazakhstan No. 574-II "On Inland Water Transport" of 6 July 2004.

39. For shipping in the Caspian Sea, the following legal regimes apply: According to the special regime on the Caspian Sea; only 5 flags (the Caspian region states) are allowed to ship in the Caspian Sea; in accordance with paragraph 3-1 of Article 11 of the Law No. 284-II "On Merchant Shipping", the right to fly the State Flag of the Republic of Kazakhstan is given to ships, operating in the property of i) the state; ii) citizens and legal entities, registered in accordance with the legislation of the Republic of Kazakhstan; and iii) foreign legal entities, operating in the Caspian Sea, in accordance with the Production Sharing Agreement (contracting companies, operators, agents).

40. Law No. 422-V of 24 November 2015 "On amendments and addenda to certain legislative acts of the Republic of Kazakhstan on the issues of non-performing loans and assets of the second-tier banks; on rendering financial services and activities of the financial institutions and the National Bank of the Republic of Kazakhstan".

41. Footnote by Turkey: The information in this document with reference to "Cyprus" relates to the Southern part of the Island. There is no single authority representing both Turkish and Greek Cypriot people on the Island. Turkey recognises the Turkish Republic of Northern Cyprus (TRNC). Until a lasting and equitable solution is found within the context of the United Nations, Turkey shall preserve its position concerning the "Cyprus issue".

    Footnote by all European Union member states of the OECD and the European Union: The Republic of Cyprus is recognised by all members of the United Nations with the exception of Turkey. The information in this document relates to the area under the effective control of the Government of the Republic of Cyprus.

42. The list of offshore jurisdictions is established by Resolution No. 145 dated 2 October 2008 of the Board of Agency of Republic of Kazakhstan on Regulation and Supervision of Financial Market and Financial Organisations "On approval of the list of offshore zones for the purposes of banking and insurance activities, activities of professional participants of securities market and other licensed types of activities in the securities market, activity of accumulative pension funds and joint stock

investment funds", as amended.{p1}As of July 2016, the list of offshore centres mentioned "1. Principality of Andorra. 2. The State of Antigua and Barbuda. 3. The Commonwealth of the Bahamas. 4. The State of Barbados. 5. The State of Belize. 6. The State of Brunei Darussalam. 7. The Republic of Vanuatu. 8. The Republic of Guatemala. 9. The state of Grenada. 10. The Republic of Djibouti. 11. The Dominican Republic. 12. The Republic of Indonesia. 13. Spain (in the part of the territory of the Canary Islands). 14. The Republic of Cyprus. 15. The Peoples Republic of China (in the part of the territories of special administrative regions of Macau and Hong Kong.). 16. The Federal Islamic Republic of the Comoros.17. The Republic of Costa Rica. 18. Malaysia (in the part of the territory of Labuan enclave). 19. The Republic of Liberia. 20. The Principality of Liechtenstein. 21. The Republic of Mauritius. 22. Portugal (in the part of the Madeira Islands). 23. Republic of Maldives. 24. Republic of Malta. 25. The Republic of the Marshall Islands. 26. The Principality of Monaco. 27. The Union of Myanmar. 28. The Republic of Nauru. 29. Netherlands (in the parts of the island of Aruba and dependent territories of Antilles). 30. Federal Republic of Nigeria. 31. New Zealand (in the parts of the Cook Islands and Niue). 32. The Republic of Palau. 33. The Republic of Panama. 34. Samoa. 35. The Republic of Seychelles. 36. The State of Saint Vincent and the Grenadines. 37. The Federation of Saint Kitts and Nevis. 38. The State of St. Lucia. 39. The United Kingdom and Northern Ireland (for the following territories: The islands of Anguilla; Bermuda Islands; British Virgin Islands; Gibraltar; Cayman Islands; the Island of Montserrat; Turks and Caicos Islands; Isle Of Man; and Guernsey, Jersey, Sark, Alderney). 40. The USA (for the territories of the US Virgin Islands, Guam and the Commonwealth of Puerto Rico). 41. The Kingdom of Tonga. 42. The Republic of the Philippines. And 43. The Democratic Republic of Sri Lanka."

43. Articles 29 and 17 of the Banking Law No. 2444 adopted on 31 August 1995, as amended, and Resolution No. 385 of the National Bank of Kazakhstan (24 December 2012), as amended; Articles 33 and 21 of the Law on insurance companies No. 126 (adopted on 18 December 2000), as amended.

44. Law on Securities No. 461 adopted on 2 June 2003, as amended, and Law on investment funds No. 576, adopted on 7 June 2004, as amended.

45. "Rules and conditions for Hiring Foreign Workers" as attached to Resolution of the Government No. 45 of 13 January 2012.

46. Law No. 574-II "On Internal Water Transport" of 6 July2004; Law No. 284-II. "On Commercial Navigation" of 17 January, 2002.

47. Law of the Republic of Kazakhstan No. 339-IV "On Use of Air Space and Air Operations" of 15 July 2010.

48. Law No. 195-I "On Advocacy" of 5 December 1997; Law No. 155-I "On Notariat" of 14 July 2007; Patent Law No. 427-I of 16 July 1997; Law No. 261-IV «On Enforcement Proceedings and Bailiff Status» of 2 April 2010.

49. The position of a forensic expert in forensic enquiry bodies can only be taken by a Kazakh citizen (Law No. 240-IV "On Forensic Examination Activity in the Republic of Kazakhstan" of 20 January 2010); The property and business of insolvent debtors as part of bankruptcy procedures can only be managed by citizens of Kazakhstan (Rules of licensing and qualification requirements to management of property and business of insolvent debtors as part of bankruptcy procedures are approved by the Order of the Government of the Republic of Kazakhstan No. 615 of 20 July 2007); only a citizen of the Republic of Kazakhstan can work as a guide (interpreter guide) or tourism instructor (Law No. 211-II "On Tourist Activity in the Republic of Kazakhstan" of 13 June 2001).

50. Law "On Public Procurement" No. 434-V dated 4 December 2015, which entered into force on 1 January 2016 and replaces the previous law "On Public Procurement" No. 303-III dated 21 July 2007. Similarly, the other legal and regulatory acts that govern public procurement do not provide for any kind of discrimination between domestic and locally-established foreign controlled enterprises.

51. Subparagraph 31 of Article 2, and Article 14 of the Law "On Public Procurement" No. 434-V dated 4 December 2015.

52. Article 193 of the Entrepreneurial Code of Kazakhstan dated 29 October 2015, effective from January 2016.

53. Article 3(15) of the Law "On Natural Monopolies and Regulated Markets" No. 272-I dated 9 July 1998, which states that "natural monopoly shall mean the condition of services (goods, works) market, where the creation of competitive conditions for satisfying demand for a particular type of services (goods, works) is impossible or economically inefficient due to the technical peculiarities of production and provision of the given type of services (goods, works)." Changes to this Law were introduced by Law No. 312-V of 5 May 2015 "On Introduction of Amendments and Additions to Certain Legislative Acts of the Republic of Kazakhstan regarding Natural Monopolies and regulated Markets" but did not affect the definition of natural monopolies.

54. The Committee on Regulation of Natural Monopolies and Protection of Competition of the Ministry of National Economy of Kazakhstan (KREMZK), as successor of the Agency of the Republic of Kazakhstan On Regulation of Natural Monopolies, maintains a Register of entities operating as natural monopolies, with the exception of those falling under the remit of the Committee on Communications, Information Technologies and Information of the Ministry for Investments and Development (post and telecommunication services). The Register maintained by KREMZK consists of a Republican (for most important companies) and Local sections (for local level companies).

55. E.g. the 2010 Subsurface Law (Law No. 291-IV adopted on 24 June 2010), as amended. See Articles 61 to 74 on subsurface users' contracts.

56. E.g. the Government Resolution No. 693 of 17 July 2008 "On Establishment of a specialised organisation on concessions", setting up the Kazakhstan Public-Private Partnership Centre ("PPP Centre"). On the PPP Centre's role, see Chapter 5 on investment promotion and facilitation.

57. List of objects which cannot be transferred into concession (Decree of the President No. 294 adopted on 5 March 2007). Kazakhstan nevertheless allows the concession of water management facilities (water intake facilities, pumping stations, water treatment facilities) of most large cities.

58. For example, in 2014, one concession relating to the construction of a 66 km ringroad around Almaty was meant to attract foreign investors to manage, maintain, and operate the new road for 20 years. EBRD, "Milestone Kazakh PPP's event at EBRD attracts over 100 companies", November 2014.

59. World Bank (2015), "International Bank for Reconstruction and Development Programme Document for a Proposed Loan in the Amount of USD 1 Billion to the Republic of Kazakhstan for the First Macroeconomic Management and Competitiveness Programmatic Development Policy Loan" (9 October 2015).

60. Between 1991 and 2005, Kazakhstan held six two-year privatization programmes. During that period, more than 39 000 state-owned enterprises were privatised with total proceeds amounting to KZT 347 billion (OECD, 2012). From 1991 to 2012,

a total of 45 631 entities, or approximately 85% of state property, were privatized (WTO, 2015).

61. Maslov D. "Privatization in Kazakhstan: losses and achievements", *Continent,* Vol. 11, 8-21 December 1999 (in Russian) (Маслов Д. Приватизация в Казахстане: потери и приобретения. // Континент. No. 11, 8-21 декабря 1999).

62. For instance, according to Kazakhstan's president Nazarbayev, the largest state owned conglomerate – National Welfare Fund "Samruk-Kazyna"– controlled at the end of 2015 a network of more than 500 subsidiaries. Other examples include the National Managing Holding "KazAgro", which is aggregating assets in the agrarian sector; the National Managing Holding "Baiterek", active in development and high-tech; and the National Information Technology Holding "Zerde", which covers communications and IT.

63. "Kazakhstan in the new global reality: growth, reform, development", address by President Nazarbayev, 30 November 2015: *http://consulsinwales.org.uk/archives/2984*.

64. Government Decree No. 1141 of 30 December 2015 "On Several Issues Related to Privatisation for 2016-2020", which entered into force on 1 January 2016. Of the 783 assets to be transferred to the private sector, 217 belong to Samruk-Kazyna and 61 are organisations owned by the central government, while 137 are subsidiaries of national managing holdings, national holdings, national companies (including socio-entrepreneurial corporations). The remaining assets are controlled by municipalities. Source: Kazakhstan's Replies to the OECD Questionnaire (June and December 2016). The government made available in 2016 the list of assets of Samruk-Kazyna to be privatised, as well as the Uniform Rules of Sale of Assets, which regulate the order of privatization of the Samruk-Kazyna's assets on the following websites: *www.sk.kz*; *www.privatization.sk.kz* and *www.skc.kz*.

65. A full list of the state-owned enterprises put up for privatisation and offered to transfer to the private sector, can be found here: (in Russian): *http://economy.gov.kz/upload/Files/Celevie_indikat_real_komp_plana_privatiz_na_2016-2020g_ru.doc*.

66. In his State of the Nation speech on 30 November 2015, President Nazarbayev stated that the "government had been instructed to create conditions for the maximum participation of local and foreign investors".

67. GRATA International, "Kazakhstan's Privatisation Decree", in *Tengri News*, 4 April 2016.

68. In particular, amendments to the Law "On Auditing" enacted in December 2011 have subjected all SOEs to statutory audits.

69. For this reason, with the entry into force of the new Law "On the State Audit and Financial Control" in November 2015, audits of SOEs will now be conducted by private auditing firms.

70. On 1 November 2016, the Ministry of National Economy issued a decree whose purpose is to bring the Kazakhstan corporate governance framework more into line with the OECD standards (Decree of the Minister of National Economy No. 465 of 1 November 2016).

71. Government decision of 25 September 2014.

72. Article 163 of the Entrepreneurial Code defines the competition authority as a state agency responsible for restricting and controlling monopolistic activities as well as for the development of competition policy by advising the government on this matter.

73. Article 4, Japan-Kazakhstan IIA (2014).

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Chapter 3

The policy framework for the balancing of investor protection and the government's power to regulate

This chapter looks at the policy framework for investment protection at the domestic and international level. A key focus is on the balancing between investor protection and the government's power to regulate. The chapter analyses protection provisions available to all persons in the general laws and those available only to investors in specific legislation, such as certain provisions under the Entrepreneurial Code. The issue of regulatory stability is addressed separately, both for contracts and investments generally and for investments in the subsurface sector in particular. The chapter also provides an overview of dispute resolution mechanisms, such as the Kazakh court system, arbitration, and mediation, and analyses recent reform efforts. Finally, the chapter analyses Kazakhstan's investment treaties and dispute settlement under these treaties, identifying options for their review.

The restrictions and conditions faced by foreign investors, both when they first establish their investment and in their on-going operations, is only one part of the overall investment environment. Transparency and predictability, non-discrimination, and the protection of property rights, combined with effective enforcement mechanisms are important pillars of a sound investment climate. Investment protection therefore plays a crucial role for the investment climate. The term describes relevant provisions and policies which define the rights of investors, and in particular the level of treatment they may expect in their dealings with the government.

Investment protection policy involves efforts to achieve a balance between investor protection and governments' right to regulate. Protection of investors from improper treatment can lower their perception of risk for new investments, and investors who perceive lower risks will generally make capital and resources available at a lower cost. At the same time, governments need latitude to regulate investment and to address evolving situations through changes in policy over time. Reconciling these goals involves a challenging process of balancing through a potentially wide range of policy tools.

A first level of protection for investors is under laws and procedures that apply to people, as well as businesses generally. The rights and interests of investors can be protected by different legal instruments, such as Kazakhstan's Constitution and different laws and regulations that apply to all persons. They are also protected by a range of administrative law doctrines as well as by good administrative practices. In many advanced economies, these are the principal protections applicable in practice to most investors under domestic law.

A second level of treatment under review here involves laws in Kazakhstan that apply specifically to investors and investments, or to some investors and investments, and that provide them with additional protection. Many emerging economies provide for additional protections for all or defined categories or investors or investments. These laws can provide important protections to some or all investors, make protections easier to identify for the relevant investors, and consequently encourage additional investment. A new Entrepreneurial Code seeks to achieve greater coherence in this area in Kazakhstan and is discussed below along with sectoral legislation. At the same time, to the extent that these laws provide rights for investors that are not available to other constituencies affected by investment, they can affect the relative influence of different constituencies on government policy.

In addition to domestic law, investment treaties or international investment agreements (IIAs) between Kazakhstan and other countries can provide additional protection to foreign investors covered by the treaties. The second section below addresses Kazakhstan's treaty network and treaty policy.

Since the OECD *Investment Policy Review* of 2012, the Kazakh authorities have introduced reforms to improve Kazakhstan's framework for investment protection. Policy reform on the national legal framework, aiming to increase the consistency and transparency of the applicable legal rules and thereby strengthen investor confidence, is underway. The new Entrepreneurial Code and current efforts to improve the rules applicable to investments in the Subsurface sector, for example, testify to this dynamic. In the field of enforcement and dispute resolution, the authorities have introduced new institutions and mechanisms, with the overall objective of providing investors with effective recourse to protect their rights. The Kazakh authorities also intend to modernise their policy on international investment agreements.

The national policy framework

General national law regulating and protecting all persons

The Kazakh authorities have undertaken efforts to improve the general rule of law and consequently the policy framework for investment. "Ensuring the Rule of Law" is a key pillar of the 100 steps set out by Kazakhstan's president to implement institutional reform. As outlined in Chapter 5, an attractive investment climate facilitating new investment and retaining existing investment depends to a large degree on sound administrative procedures and high quality regulations. Predictability and coherence in the government's regulatory activity enhance investor confidence, particularly when they are accompanied by consistent applications of the rules in force. These elements, which in themselves constitute important assurances for investors, are complemented by provisions in the general national law ensuring additional protection that also apply to investors.

The Constitution provides that the scope of property rights and guarantees of their protection shall be determined by law. It also specifies that "[p]roperty shall impose obligations, and its use must simultaneously benefit the society."[1] These provisions would appear to provide for a degree of protection against illegal measures affecting property. They would appear to provide limited protection against changes in the law that restrict the scope of property rights or other regulatory changes. The Constitution also generally provides for non-discrimination.[2] While these constitutional principles are important, they appear to play a less immediate role in practice than more specific legislative provisions protecting investors as discussed below.

The Entrepreneurial Code: specific legislation regulating and protecting certain investors and investment

The Entrepreneurial Code (EC)[3] entered into force in 2016 and replaces the previous Investment Law, and other laws regulating and protecting business activity (Dentons, 2015). It aims to increase the consistency and transparency of the applicable legal rules for businesses,[4] and investors specifically, and to thereby strengthen investor confidence.

The EC grants all investors protection against direct expropriation, referred to as "nationalisation and requisition". It provides that seizure of property is only permitted in exceptional cases stipulated by legislative acts and that compensation has to be paid.[5] In case of nationalisation, the investor shall receive full compensation for the damages sustained. The investor shall receive the full market value in case of requisition,[6] which is to be determined in accordance with the legislation.[7]

From the provisions it is not clear whether cases of indirect expropriation are covered, i.e. cases where the investor still holds the property title but where government measures have an impact on the property which is considered to be tantamount to expropriation (see below section on "indirect expropriation" under international investment agreements).[8]

The EC provides generally that investors can obtain damages as compensation for illegal government action or inaction.[9] Article 276 provides that investors are entitled to compensation for harm caused by unlawful statutes, and unlawful action or inaction by the Kazakh authorities.[10] In contrast to this approach, damages remedies for investors for illegal government action are generally used sparingly under the administrative law of advanced economies, which instead favour non-pecuniary remedies such as annulment or injunctions (Gaukrodger and Gordon, 2012: 24-29; OECD, 2012b).

The EC investment definition is relatively broad, including all types of property. However, the EC also introduces distinctions between different categories of investors and investments with different legal rights. For example, only investments that meet certain criteria, and/or are placed on administrative lists, qualify for some benefits, in particular relating to the stability of the legal framework (see below).[11]

These complexities can raise a number of issues. In general, Kazakhstan should seek to provide a sound investment climate for all investors in order to ensure that capital is efficiently allocated to its most valuable uses in the market rather than being allocated in light of administrative benefits. Multiple categories of treatment may also give rise to disputes about whether particular investors or investments fall into the specially protected categories. The additional costs of special regimes for different types of investors/investment should generally only be incurred where they are justified by a

strong need to encourage particular, well-defined types of investment and where the costs of treating all investors the same are excessive.[12]

Protection and enforcement of intellectual property rights

The granting and protection of intellectual property (IP) rights, e.g. through patents, trademarks, and their enforcement are an important component of any policy aiming at attracting investment. Protection of IP rights also fosters development and innovation (OECD, 2016a). The protection of IP rights also involves balancing issues: While IP rights provide an incentive to invest in research and development, societies have an interest in having new products priced affordably.[13] High levels of IP protection might impede access to pharmaceutical products at affordable prices, for example.

Kazakhstan's main legal instruments on IP rights include the Civil Code, the Patent Law from 1999, and the Law on Copyrights and Neighbouring Rights from 1996. Kazakhstan has also signed and ratified a number of international IP agreements, including agreements under the WTO, such as the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS).[14]

The legal framework for IP rights in Kazakhstan has evolved considerably since the country gained independence in 1991. While the 2012 OECD *Investment Policy Review* described several changes to the legislative and institutional landscape improving the protection and enforcement of IP rights, the enforcement in particular was identified as an area where domestic and foreign operators expressed concerns. Additional changes have occurred in the context of Kazakhstan's accession to the WTO. In the 2015-16 period alone, six of the main IP laws were amended.[15]

Protecting different types of IP rights

Patents can be obtained at the national level by filing an application with the patent office of Kazakhstan. In line with international practice, the authorities undertook in 2016 a comprehensive assessment of Kazakhstan's compliance with the novelty and inventiveness requirements (OECD, 2016a). The protection of minor innovations can be a stepping stone towards patenting: since the amendment of the Patent Law in 2015, so-called utility models allow for such applications. For utility models, there is only a novelty but no inventiveness requirement. Obtaining this type of IP rights needs to be more time-efficient, less cumbersome and less costly in order to be an attractive alternative to patents (OECD, 2016a). Information by Kazakhstan's National Institute for Intellectual Property (NIIP) shows that the cost for a utility model application is 20% lower than for invention patent application (OECD, 2016a: 80).

Kazakhstan has also adhered to several instruments at the international level that facilitate the filing of patents. Together with Armenia, Azerbaijan, Belarus, Kyrgyzstan, Russia, Tajikistan, and Turkmenistan, Kazakhstan is a member of the Eurasian Patent Organisation (EAPC), which provides for a single patent application procedure. Compared to the application numbers under the national system, the patents filed under EAPC are relatively low (OECD, 2016a: 81). As a member of the Patent Co-operation Treaty, patent applicants can seek protection in all member countries simultaneously.

Specific rules apply to the protection of intellectual property rights in individual areas, such as industrial design, trademarks and appellation of origin, or copyright.[16] The Ministry of Healthcare and Social Development is involved in some areas, such as compulsory drug licences. Changes implemented in the WTO accession process include increased protection for pharmacy companies' of new types of medicine; and modified provisions on the possibility of issuing compulsory licences (OECD, 2016a: 85).

Improving the enforcement of IP rights

Enforcement of IP rights continues to be a challenge and constitutes a policy priority for Kazakhstan (OECD, 2016a: 14). Kazakhstan's laws provide for the enforcement of IP rights both through civil and criminal proceedings. In civil cases, remedies include injunctions, damages, and accounts of profits. Criminal sanctions under the Criminal Code include fines, correctional work, public works, arrest and imprisonment. The Administrative Code provides for the administrative liability of IP rights infringement, including through fines and the restitution of goods (OECD, 2016a: 75). In addition to the courts, the customs authorities are also involved in the protection of IP rights.

These enforcement mechanisms, however, do not appear to be used effectively yet. The United States noted in their 2015 report on trade barriers that while some efforts have been taken by Kazakhstan, there was a need for applying more effectively customs control against imported IP rights-infringing goods (United States, 2015: 230). The United States also noted that although civil courts have been used effectively in IP rights enforcement, judges often lack technical expertise (United States, 2015: 232). In light of the low number of cases, improving capacity of judges appears to be a better option than creating a special court for IP rights enforcement (OECD, 2016a: 68). The ongoing efforts to improve the functioning of the Kazakh court system and to enhance capacity of judges (see sections below as well as Chapter 5 on investment facilitation) suggest that the authorities are taking the issue seriously.

Regulatory stability and balancing efforts

A substantial degree of regulatory stability is a key element of a good balance between investment protection and the right to regulate

The OECD *Policy Framework for Investment* recognises that predictability is a key concern for investors. In March 2014, the Kazakh President underlined the importance of the stability of contracts and legislation for the investment climate.[17] As noted throughout this report, Kazakhstan has engaged in numerous reforms. While reforms are necessary and valuable in many areas, it is important to bear in mind that regulatory change imposes costs and that repeated changes in particular can cause uncertainties and compliance costs. Regulatory stability has value in itself and should be included in the cost/benefit analysis for new regulation.

Beyond inclusion of restraints on regulatory change as a matter of good general regulatory practices, specific government commitments to provide regulatory stability, through stabilisation clauses in contracts or legislative provisions, may be a tool to increase investor confidence. Specific commitments for regulatory stability should not, however, be seen as a permanent substitute for a broadly sound legislative and regulatory environment. Research suggests that OECD member countries, with high rule of law standards, generally refrain from offering investors specific stability assurances. Where they offer stability assurances, these are typically much narrower than in countries with weaker governance and rule of law standards (IFC, 2009). This suggests that stability assurances are not necessary for an attractive investment climate if the overall legal framework provides for the rule of law and sufficient predictability. As a general matter, they should best be seen as a useful policy to increase investor confidence until an improved overall legal framework ensures adequate predictability and protection for investors.

Stability commitments need to be used carefully. They directly constrain the government's future ability to regulate economic activity. For example, tax policy designed to encourage particular outcomes – such as decreased consumption of carbon – will be of limited effect if the government must indemnify investors for the increased taxes. Where stability commitments are provided to some investors and not others, they can affect competitive conditions. By their nature, they also apply differently to different investments made at different times, and consequently create high levels of legal complexity.

Many emerging economies provide for a regime for stabilisation commitments for certain types of contracts or investments in legislation.[18] This allows the legislature, rather than individual officials, to define the proper scope of stabilisation commitments. The application of the regime to particular contracts or investments is then agreed upon or not in the context of the

specific negotiations. This allows the government to limit the application of stability commitments – and the consequent exposure to damages including for regulation needed in the future – to contracts and investments where they are necessary. Kazakhstan appears to have applied a more general regime of commitments that apply automatically to all contracts or investment of particular types. This may lead to a large number of stabilised arrangements.

Government commitments on stability in the Entrepreneurial Code

Stability commitments can apply to contracts or more broadly to investments. The EC contains both types.

Article 276(3) of the EC contains a stability commitment for investor-state contracts. However, its operation is not fully clarified. The law states only that Kazakhstan guarantees the stability of contracts between investors and state bodies. The notion of stability is not defined.[19] Moreover, although there are specific dispute resolution provisions for such contracts (see below the statutory regime for "Investment Disputes" as defined), remedies for breach of the stability commitment are not specified.

The Code provides for exceptions for the fields of import, production, sales of excisable goods restrictions,[20] national security, health and morality.[21] The important issue of environmental regulation, however, is not addressed clearly. The previous Investment Law contained an express exception for environmental measures, but the EC does not. Some environmental measures could conceivably be covered under general headings such as national security[22] or health, but such coverage is unclear. The Kazakh authorities have explained that environmental measures do fall under the national security exception.[23]

The EC also provides for stability commitments for certain investments. A section on "State investment support" contains stability provisions applicable to two types of legislation: i) tax legislation; and ii) legislation "on employment in the field of attracting foreign labour".[24] Protection from change to tax and foreign employee legislation under this regime applies to the investment as a whole rather than to only the investor-state body contract. The impact of regulation on other contracts and aspects of the investment can thus be taken into account.

Only some investments, however, qualify for this stability assurance: "priority investment projects" and "strategic investment projects". "Priority investment projects" are defined as those carried out by newly established legal entities with activities defined in a list approved by the government and having a certain volume. "Strategic investment projects", defined in a list, are able to "exert strategic influence on the economic development" of Kazakhstan.[25] The list, approved by government decree in 2009, is not subject to any changes, according to the Kazakh authorities.

Government commitments on stability to the extractive industries

Article 30 of the Kazakh Law of Subsurface and Subsurface Use (Subsurface Law) from 2010 provides that investors in this sector shall be guaranteed protection of their rights under the laws of Kazakhstan and that changes and additions to legislation which adversely affect entrepreneurial activity do not apply to contracts entered into prior to making these changes and additions. The Subsurface Law includes carve-outs for legislation relating to national security, defence, environmental safety, health, taxation and customs regulation.

The Kazakh government is currently preparing a new Subsurface Use Code to replace the Subsurface Law. Although earlier reports suggested that the new Code would exclude stabilisation commitments, a preliminary February 2016 draft of the Code still contains stabilisation provisions. Under the draft, legislation which comes into force after the investor's rights are granted, and which detrimentally affects the investor's situation, would not apply to the investor. Carve-outs apply for national security, defence, environmental and industrial safety, health care, taxation and customs regulation.[26] Issues that appear to be raised by the new draft include defining the meaning of a detrimental effect on the investor's "situation", coverage of environmental legislation, and the advisability of automatic application to all new Subsurface investments given the resulting complexity and government liability exposure.

Box 3.1. **Ongoing reform efforts affecting the legal framework for investment in the extractive industries**

The natural resources sector plays an important role for the country's economy. This box addresses selected aspects and changes in the legal framework which are relevant for the extractive industries:

- Transparency and corruption

The natural resources sector is often seen at the centre of challenges relating to corruption and a lack of transparency. This sector is also the focus of important initiatives, such as the *Extractive Industries Transparency Initiative* (EITI). The EITI Standard requirements include transparency of the legal framework and disclosure of relevant information on exploration and production, company payments and government revenues, revenue allocations, social expenditures and the impact of the extractive sector on the economy. Kazakhstan participates in EITI and according to the EITI website, is compliant with requirements set out in the EITI Standard. Increased transparency in this sector is also one of the explicit goals of the 100 steps set out by the Kazakh President Nursultan Nazarbayev to implement institutional reform (see Step 74). In addition to helping combat corruption, transparency can contribute to foster investor confidence and stakeholder dialogue.

Box 3.1. **Ongoing reform efforts affecting the legal framework for investment in the extractive industries** *(cont.)*

- Diversification of the Kazakh economy, local content requirements, and the WTO accession process

Previous OECD work points out that oil-based growth, for example, poses challenges for macroeconomic and financial sector stability and the development of the non-oil economy (OECD, 2016b: 94). Ongoing diversification efforts notwithstanding, the Kazakh economy still relies heavily on the natural resources sector (OECD, 2016b: 118). The legal framework for investment in this sector can have an important impact on diversification efforts: It appears that many of Kazakhstan's investment contracts in the extractive industries contain so-called "local content requirements", which can oblige the investors to use for example local personnel or products.

The WTO accession reduces the opportunity for using such a policy tool (see sections on local content policies in chapter 2). In addition, some of Kazakhstan's existing international investment agreements place limits on performance requirements such as local content requirements.[27] Such requirements in future investment contracts must be tailored in light of these new obligations. A transition period seeks to ensure the effectiveness of commitments undertaken in existing contracts (Dentons, 2015).

Kazakhstan has also established mechanisms, such as the National Fund of the Republic of Kazakhstan (NFRK), which seek to ensure that the revenues of the natural resources sector are well-managed and used to allow a diversification of the economy.

- International co-operation on extractive industries

The draft Subsurface Use Code from 2016 contains a reference to international co-operation,[28] through which the country seeks to benefit from other countries, as well as international organisations, to create an environment favourable for investment and modern technologies. International agreements, such as the Agreement between the Government of the Federal Republic of Germany and the Government of the Republic of Kazakhstan on Partnership in the fields of Raw Materials, Industry and Technology from 2012, already testify to such co-operation efforts. According to the German government, the agreement seeks to facilitate the access of German companies to natural resources and will also be linked to a contribution from German firms to the industrialisation of Kazakhstan (German Ministry for Economic Affairs and Energy, press release, *www.bmwi.de/EN/Press/press-releases,did=474976.html*). According to information provided by the Kazakh authorities, the co-operation under the agreement has led to more than 25 investment projects by German companies.

Dispute resolution: the national framework and commercial arbitration

The balancing between investor protection and government's power to regulate is also at issue in policies relating to dispute settlement.[29] For businesses operating in Kazakhstan, it is important to have well-functioning contract enforcement and dispute settlement mechanisms because they help increase predictability in commercial and investment activities. The court system has a fundamental role in enforcing contracts and in settling disputes, both among private actors and between an investor and the state. In addition to the court system, businesses may rely on commercial arbitration, and other alternative dispute resolution mechanisms. The identity and characteristics of adjudicators in different systems may have important consequences for the relative importance that is accorded to investor protection and the power to regulate in concrete cases (which can also create precedents for the future).

The EC generally grants businesses the right to recourse before the Kazakh courts under the procedures established by the Civil Procedure Code (CPC).[30] The EC also provides for a wide range of alternative dispute resolution mechanisms, including arbitration and mediation.[31]

The EC again provides a special regime for "Investment Disputes", defined as those arising out of contracts between an investor and a state body. Generally, Investment Disputes can be resolved by negotiation or by dispute settlement methods agreed by the parties.[32] If the parties fail to settle the dispute by negotiation or the mechanisms agreed upon by the parties, the dispute shall be settled in accordance with any applicable international treaties and the applicable laws of Kazakhstan.[33]

The domestic courts

There are conflicting reports on the quality of Kazakhstan's courts although there is evidence of improvement. According to the World Bank's *Doing Business* report, contract enforcement and dispute settlement in domestic courts is an area where Kazakhstan has improved substantially over the last years – it now stands 9 in the ranking of 189 economies surveyed (World Bank, 2016: 85).[34] The World Bank's *Enterprise Survey* results from 2013 showed that only 10% of foreign-owned firms saw the court system as a major constraint and business obstacle. However, other indicators suggest that investors often remain concerned about the reliability of domestic courts and the rule of law. According to EBRD information from 2014, the bank's *Judicial Decisions Assessment* found that the quality of commercial judgement was uneven and that "courts are believed to show particular deference to the government and entities in which the state has a substantial interest" (EBRD, 2014: 4). Discussions with stakeholders in Kazakhstan appear to corroborate these findings. Discussions with stakeholders also suggest that problems are largely limited to the lower level courts and that

appellate courts and the Supreme Court have both better quality proceedings and higher levels of independence. The functioning of the lower courts is an area where *Doing Business* report observed improvements.

A new Code of Civil Procedure, which entered into force on 1 January 2016, is one pillar of recent reform efforts. It introduces important changes to the judicial landscape and the functioning of the court system. In line with the 100 steps set out by the President to ensure the rule of law, the Code establishes a "stream-lined" three-tier court system. The system now consists of trials courts at the level of first instance, appellate courts (the courts of Astana and Almaty have an appellate function), and the Supreme Court.

Pursuant to art. 82 of the Constitution, judges are appointed by the President of Kazakhstan. The President also plays a key role in the appointment of the members of the Supreme Judicial Council itself (GRATA International, 2016b). The Kazakh authorities have emphasised that a new law on the Supreme Judicial Council, which entered into force on 1 January 2016, modified the functioning and role of this institution, giving it a more important role in the appointment and promotion processes of judges.

Kazakhstan is also seeking to improve the quality of its judicial personnel. The Law of Judicial System introduces new criteria for the appointment of judges: the required work experience is increased from 2 years to 5 years (for those already working in the judicial system) and 10 years for practicing lawyers. For judges at the Supreme Court, 20 years of work experience are required, at least 10 of which as judges and 5 as judges at a regional court. The performance of the judges is generally reviewed every five years by a Court Jury. An Academy of Justice has been established to foster capacity-building and training activities (GRATA International, 2016a).

The special regime for Investment Disputes provided for in the EC (see above) is further specified in the Code of Civil Procedure. A dedicated panel of judges at the Court of Astana will hear Investment Disputes. The Court, however, is only competent if the parties have not agreed to settle the dispute through other mechanisms.[35] Disputes involving "major investors", defined in the EC as those with a minimum amount of investment, will be heard by a dedicated division of the Supreme Court, unless agreed otherwise by the parties (Baker & McKenzie, 2015).[36] While there can be value in offering dedicated venues for certain disputes, Kazakhstan might wish to consider whether jurisdiction should be defined by classes of disputes rather than classes of investors.

Alternative dispute resolution mechanisms

The additional alternative dispute resolution mechanisms in the CPC, further specified in the Law on Mediation from 2011 (No. 401-IV), and the Law

on Arbitration from April 2016 (No. 488-V SAM, "Arbitration Law"), are reportedly intended to reduce the case load of the Kazakh courts.[37]

Commercial arbitration. The legal framework for arbitration has changed considerably since the last *Review*, most recently with the Arbitration Law which entered into force in April 2016. The new law consolidates the Arbitration Tribunal Law and the International Arbitration Law from 2004, applicable to domestic and international arbitration respectively.

The Law defines which disputes can be brought to arbitration and lays out the formalities that the parties have to follow in their arbitration agreements.[38] Moreover, it contains provisions on the composition of the arbitral tribunals and requirements to be met by the arbitrators.[39]

The Arbitration Law provides for arbitration between private parties. It also allows for arbitration between private parties and state entities (such as governmental authorities, states enterprises, and legal entities where the state owns more than 50% of the voting shares). In this case, arbitration is subject to approval by the relevant government agency or authority.[40] The effectiveness of this type of provision in national law should not be over-estimated. Arbitrators in international commercial arbitration cases have frequently refused to allow governments to invoke this type of provision to block arbitration if a government official has signed a contract providing for arbitration (Born, 2014: 727-733).

For disputing parties it is important to know that decisions and awards of arbitral tribunals will be enforced. The Arbitration Law notably provides that when an international treaty establishes rules other than those found in the laws of Kazakhstan, the rules of the treaty shall apply. Kazakhstan is a party to the Convention on the Recognition and Enforcement of Foreign Arbitral Awards (also called New York Convention), the leading international treaty applicable to commercial arbitration. The New York Convention addresses the recognition and enforcement of foreign arbitral awards (i.e., those made in a country other than Kazakhstan) and for certain awards made in Kazakhstan.[41] The national courts of contracting parties to the New York Convention must generally recognise arbitration awards rendered in other contracting parties, subject to narrow exceptions, and enforce the awards in accordance with their rules of procedure. Since Kazakhstan is a contracting party to the New York Convention, investors that have prevailed in arbitral proceedings against Kazakhstan know the conditions under which the awards will be recognised and enforced in Kazakhstan. The New York Convention also facilitates the recognition and enforcement of Kazakh awards in third countries that are party to it.

The Arbitration Law further provides for the establishment of a Chamber of Arbitration. While the primary purpose of the Chamber is to strengthen

arbitration as a dispute resolution mechanism under the laws of Kazakhstan, it also has logistical support functions for arbitral proceedings.[42] High-profile recent arbitration cases reported on in the press suggest that arbitration is of practical relevance, not only for disputes among businesses, but also for the government in its dealings with businesses operating in Kazakhstan (CNBC, 2016).

Mediation. Despite the adoption in 2011 of a Mediation Law (28 January 2011 No. 401-IV), mediation does not appear to be often used in Kazakhstan. The 2016 reforms of the Entrepreneurial and Procedural Codes seek to further promote mediation as an alternative dispute settlement mechanism. Court-assisted mediation proceedings, in which judges can be requested by the parties to assist them in their mediation efforts, are actively promoted. The judges' role is then to review and approve a mediation agreement (CIS Arbitration, 2016). As reported above, one of the rationales behind these mediation mechanisms is to reduce the case load of the courts.

The Astana International Financial Centre and its proposed autonomous court system. Building on the model of the Dubai International Financial Centre,[43] the Kazakh authorities are seeking to establish the Astana International Financial Centre (AIFC). On 7 December 2015, President Nazarbayev signed the constitutional law "On the Astana International Financial Centre" (AIFC law) (The Astana Times, 2015). The declared objective is to attract investments to Kazakhstan by creating an attractive environment for financial services; develop the Kazakh securities market and ensure its integration with the international capital markets; develop a market of insurance services, banking services and Islamic finance; develop financial and professional services based on the best international practices; and acquire international recognition as a financial centre.[44]

The AIFC will reportedly have its own autonomous court system that will use English for court proceedings, apply English law and be staffed by foreign judges. It will have jurisdiction to settle disputes involving AIFC members. This will require major amendments to the Constitution and core legislation such as the Tax Code and the CPC (Dentons, 2015).

International investment agreements

Kazakhstan has a network of international investment agreements (referred to as investment treaties or IIAs).[45] Investment treaties typically protect existing covered investments against expropriation without compensation and against discrimination, and give covered investors access to investor-state dispute settlement mechanisms (ISDS) to enforce those provisions (see Box 3.2 for common features of IIAs). Kazakhstan started

Box 3.2. **Features of international investment agreements**

IIAs, entered into between two or more countries, typically offer covered foreign investors substantive and procedural protection. They provide additional protection to covered foreign investors beyond that provided in national legal frameworks to all investors and/or to foreign investors specifically.

Substantive protections generally include protection against expropriation without compensation and against discrimination by, for example, guaranteeing that covered foreign investors will be treated no less favourably than investors from the host state (national treatment, or NT) or third states (most-favoured nation treatment, or MFN). Particularly important for policy considerations are guarantees of fair and equitable treatment (FET) or FET in accordance with the international minimum standard of treatment of aliens under customary international law (MST). The FET provision is subject to widely varying interoperations and has been the one most frequently invoked by foreign investors in recent years. Additional clauses in IIAs can facilitate the transfer of profits, or limit or exclude certain performance requirements, such as local content rules.

IIAs can also reduce barriers to investment. They can include commitments to open sectors to more foreign investment (market access).They can also give prospective covered foreign investors certain rights, typically by extending the NT and MFN standards to those seeking to make investments.

IIAs usually provide for procedural venues to enforce the host state's obligations under the substantive standards. Today, most IIAs give investors the right to bring claims themselves against the host state before international arbitration tribunals for an alleged breach of the IIA – the so-called investor-state dispute settlement mechanism (ISDS) (Pohl et al., 2012; Gaukrodger and Gordon, 2012). The number of ISDS claims under IIAs has risen significantly in recent years to over 600 known claims currently (UNCTAD, 2015). Precise numbers of the cases are difficult to establish because of the confidentiality of certain proceedings.

signing investment treaties in 1992, right after the country gained independence. In addition to 47 bilateral investment treaties, 44 of which are in force, Kazakhstan is also a party to regional and multilateral agreements. These include the Energy Charter Treaty (1994), the Eurasian Investment Agreement (2008), and the Treaty on Eurasian Economic Union (2014). The investment chapter of the Eurasian Economic Union-Viet Nam free trade agreement only applies between the Russian Federation and Viet Nam.

The sections below give an overview of selected provisions in Kazakh IIAs on the basis of a sample of publicly available treaties.[46] Kazakhstan's legal and institutional framework for settling disputes between the state and foreign

investors is also presented. While the review of the substantive and procedural provisions in Kazakhstan's investment treaties shows that the language of key treaty provisions has evolved in recent treaties, this is not the case for the majority of Kazakhstan's existing treaties.

The ongoing preparation of a new model investment treaty by Kazakh authorities could serve as an opportunity to ensure that recent practices are reflected in Kazakhstan's future agreements. In this context, Kazakhstan should also review the consistency of its existing treaties with recent approaches in international treaty policy and its investment policy. Table 3.3 below provides information on the temporal validity of Kazakhstan's investment treaties in this regard. Dates for renewal or termination of treaties should inform Kazakhstan's timetable to address its treaties with its existing treaty partners.

Degree of specification of investment protection provisions in Kazakhstan's investment treaties

International practice shows that investment protection standards in older IIAs have often been relatively vague. This gives investment arbitrators broad discretion to interpret and thereby determine the scope of protection they provide. Many provisions in Kazakhstan's existing IIAs, in particular older treaties, lack specific language to indicate government intent as to their scope and meaning.

Direct and indirect expropriation

Kazakh IIAs require host states not to expropriate unless the measures are taken in the public interest, on a non-discriminatory basis and under due process of law, with prompt, adequate and effective compensation. The relevant provisions typically address the determination and modalities of payment of compensation as well. Kazakh treaties distinguish and cover both direct and indirect expropriation.[47] Direct expropriation generally refers to an actual taking of legal title to property or a physical seizure of property by a government. As a result, the host state is enriched by, and the investor is deprived of, the value of the expropriated property.

Indirect expropriation is a more complex and sensitive issue. Regulatory action or other behaviour by a government can sometimes have a dramatic impact on an investment, without involving a formal transfer of title or outright seizure. At the same time, provisions on indirect expropriation can affect the host state's policy space because regulatory action can give rise to claims for compensation. Because most policy issues relating to expropriation arise with regard to indirect expropriation, this section focuses on Kazakhstan's policy in that area.

Unlike the national law, discussed above, most Kazakh IIAs explicitly cover indirect expropriation, but none of the treaties clarifies the circumstances under which regulatory measures do not amount to expropriation and where therefore no compensation has to be paid. This gives arbitrators discretion to draw the line between indirect expropriations that entitle the covered investor to compensation, and legitimate regulation that may have a significant economic impact on the investor without obligating the government to pay compensation. Under treaties that refer only generally to indirect expropriation, ISDS tribunals have used varying approaches to determining whether an indirect expropriation has occurred (UNCTAD, 2012).

In order to address this challenge, a growing number of countries have started to include specifications on indirect expropriation. These frequently aim to ensure that non-discriminatory measures, designed and applied to protect legitimate public welfare objectives, such as public health, safety and the environment, cannot constitute an expropriation.[48] Including a similar specification in its treaties would allow Kazakhstan to foster the balance between the government's right to regulate and investor protection, and also help increase the predictability of the legal framework for expropriation for both investors and the government.

Fair and equitable treatment and the international minimum standard of treatment of aliens

Fair and equitable treatment (FET) is another standard at the centre of investment treaty claims and treaty policy. Since 1997, investors worldwide have invoked the standard in 341 claims and tribunals have found a breach in 129 of the cases.[49] Kazakh IIAs typically grant FET to covered investors. These treaties often merely state that foreign investors shall be accorded FET without providing further specification. Provisions providing generally for FET have been considered or applied by tribunals in a broad range of claims and there have been widely different interpretations by some arbitral tribunals. Some interpretations of FET are seen as having a significant impact on the right to regulate.

Internationally, there is a growing trend to define FET provisions in treaties to give more direction to arbitrators by clarifying the original intent of the contracting parties. Two approaches to defining FET are outlined in Box 3.3 below. Efforts to include more specific language on FET do not appear to be reflected in recent Kazakh treaties.[50]

Given the centrality of FET to many investor claims and the uncertainty of its meaning, clarification of government intent could improve predictability for both governments and investors. Kazakhstan might wish to reflect the more specific language found in recent international treaty practice in its own policy.

Box 3.3. **Two approaches to specifying and limiting the FET provision**

Two important approaches to further specifying the scope of fair and equitable treatment have emerged:

- *Express limitation to the minimum standard of treatment under customary international law (MST):* This approach has been used in a number of major recent treaties in Asia and the Americas. A FET provision limited to MST has been repeatedly interpreted under NAFTA. It has been interpreted more narrowly than FET provisions under other treaties. NAFTA governments have also had much greater success than other governments in defending FET claims (UNCTAD, 2012: 61). In addition to the limitation of FET to MST, the Trans-Pacific Partnership agreement (TPP), which is a largely built on US practice, specifies that the mere fact that government action is not consistent with an investor's expectation does not constitute a breach of FET (Art. 9.6(4). Art. 9.6(3) and (5) contain further specifications).
- *Defined lists of elements of FET*: The EU's proposal for the Transatlantic Trade and Investment Partnership (TTIP), the EU-Viet Nam FTA and the CETA agreement made public in 2016, contain a defined list of elements of the FET provision. This approach lists the elements that can constitute a breach of the standard, namely denial of justice, fundamental breach of due process, targeted discrimination on manifestly wrongful grounds, and abusive treatment of investors. While it is a closed list, this approach is broader than some interpretations of MST. Arbitration tribunals cannot add new elements. Only the Parties may agree to add further elements to the list. The article also provides that the tribunal "may take into account" (or "will take into account", in EU-Viet Nam FTA) specific representations that created legitimate expectations. Other defined list approaches are also used. For example, the ASEAN-China Investment Agreement (2009) limits the application of its FET provision to cases of denial of justice (Art. 7).

Both options are more specific than the broad language of treaties that only refer to "fair and equitable" treatment. This does not mean, however, that issues of interpretation may not arise. The content of the minimum standard of treatment, for example, is subject to debate as are a number of elements in the defined EU lists.

Most-favoured nation treatment

Most of the investment treaties entered into by Kazakhstan reviewed for this report contain most-favoured nation (MFN) treatment provisions which guarantee that covered investors will not be treated less favourably than those of third states. Similarly to the other investment treaty provisions reviewed above, the Kazakh IIAs typically use general language to accord MFN treatment

to foreign investors. The meaning of general wording in an MFN clause has been subject to different interpretations. The ensuing uncertainty creates costs for governments, some of which have responded by providing more specific language on the scope of the MFN provision.

With respect to investment protection granted to nationals of third states in investment treaties, one important element is the question of whether the MFN provision only applies to substantive protection provisions – such as the indirect expropriation or FET provisions discussed above – or also to procedural aspects, and notably the ISDS mechanism (Dolzer and Schreuer, 2012). On this particular question, some countries provide more specific language, and some specifically provide that the MFN clause does not apply to ISDS available to investors under IIAs.[51] While such specifications appear lacking in Kazakhstan's investment treaties, the treaty with Japan does not specifically exclude access to ISDS from the scope of MFN, but provides that MFN applies to access to the courts of justice and administrative tribunals and agencies.[52]

Other recent international agreements provide further specifications that Kazakhstan might wish to consider: CETA provides that MFN substantive obligations in other investment treaties do not constitute treatment in themselves; only measures adopted and maintained at the domestic level constitute treatment covered by the MFN provision.[53] Some contracting parties to the TPP have specified that the MFN provision does not cover investment treaties already in force.[54] This may also help to ensure that efforts to specify investment treaty language in new treaties are not circumvented by covered investors by invoking potentially more favourable provisions included in older treaties.

Balancing the right the regulate and investor protection through exceptions clauses

Investment treaty provisions, such as the expropriation and FET provisions discussed above, affect the balance between investor protection and the right to regulate: their design, and application by tribunals, determines which government measures may be successfully challenged by investors. There is a growing recognition that some versions of FET and indirect expropriation provisions reduce the governments' policy space.

To seek to protect certain types of regulation from challenge, Kazakhstan's treaty with Japan provides for general exceptions clauses, apparently inspired from international trade law.[55] Exceptions clauses are increasingly used as a tool to help achieve an adequate balance between investor protection and governments' right to regulate. The rationale for these clauses is to ensure that the host state will not be prevented from implementing measures that pursue specific regulatory goals providing certain requirements are satisfied. Unlike

clarifications limited to a particular treaty provision, like for indirect expropriation addressed above, these provisions can protect measures that satisfy their criteria from challenge under the treaty as a whole. This type of clause, however, appears to be the exception in the Kazakh treaties.

In the treaty with Japan, the general exceptions clause is complemented by a more targeted provision relating to the financial services sector.[56]

Box 3.4. **Preserving and enforcing regulatory standards**

A growing number of investment treaties internationally make investment protection conditional on compliance with host state law. Investment treaties, among them some Kazakh treaties, use different ways to ensure that only investments that do not violate host state law are covered and protected. These include making legality a condition for application of the treaties or by defining covered investments as those made "in accordance with" host state law.[57] Several arbitration tribunals have interpreted such provisions as only applying to the time of the making of the investment but not to violations of host state law after the investment has been made. Such requirements encourage investors to be more mindful of their obligations under host state law.

Other provisions seek to influence the actions of governments themselves. In the Japan-Kazakhstan IIA, for example, both countries recognise that it is inappropriate to encourage investment by investors of the other contracting party by relaxing environmental, health, or safety measures or by lowering labour standards.[58] Practice suggests that contracting parties have rarely sought to enforce this type of commitment, which is typically subject to state-to-state dispute settlement mechanisms.[59] The absence of a venue for other stakeholders to enforce those provisions, such labour organisations for labour standards, for example, is seen as a weakness by some civil society organisations.[60]

Both the "in accordance with the law" clause and the commitment not to lower standards seek to ensure the quality of investments that are encouraged and protected by the contracting countries under the treaty.

Specifications of treaty language reflect policy choices

More specific language in investment protection provisions would lead to increased predictability and thereby benefit both investors and governments. The specifications reflect policy choices and also play a crucial role in the quest for balance between investor protection and governments' right to regulate. In some cases, the specifications may affect the degree of protection for covered foreign investors. Policy-makers need to carefully consider the costs and

benefits of these choices, and their potential impact on foreign investors and domestic investors, as well as on the host state's legitimate regulatory interests and its exposure to investment claims.

Box 3.5. **Public scrutiny and reform of international investment agreements**

IIAs have come under increasing scrutiny by a variety of stakeholders, including civil society and academia, but also by contracting parties to IIAs themselves. Critics argue that international investment agreements unduly restrict governments' "right to regulate" and that arbitral proceedings are subject to important flaws. In this process, a number of core assumptions have been challenged. Econometric studies, for example, have failed to demonstrate conclusively that IIAs actually lead to increased FDI flows – a policy goal commonly associated with the investment protection regime (Sauvant and Sachs, 2009). Furthermore, while it has been contended that IIAs advance the international rule of law and good governance in host states by providing mechanisms to hold governments accountable, critics argue that opaque legal proceedings and potential conflicts of interest of arbitrators are contrary to rule of law standards (Van Harten, 2008). Moreover, the availability of international investment arbitration to investors has been seen by some as an instrument that could circumvent, and thereby weaken domestic legal and governance institutions instead of strengthening them (Ginsburg, 2005).

Many governments are engaged in review of their investment treaty policy and the field has been marked by significant reforms in recent years. Several economies, including India and South Africa, have proposed different approaches to substantive and procedural provisions in investment treaties. Other economies, such as the European Union, have proposed new approaches to ISDS specifically (see below). At the same time, a number of countries continue to conclude investment treaties that do not reflect the recent approaches.

Reconsidering policy rationales for different levels of treatment for different types of investors

Treatment of domestic and foreign investors

In general, Kazakhstan should seek to guarantee a sound investment climate for both domestic and foreign investors. Parts of Kazakhstan's legal framework applicable to investment protection, such as the Entrepreneurial Code from 2016 (as well as the former Investment Law), apply to both domestic and foreign investors. At the same time, the country's legal framework for investment also contains many provisions, such as those found in IIAs, that

cover only some foreign investors. Kazakhstan should consider whether distortions to efficient investment decisions may occur because of more favourable regulatory conditions for certain investors based on nationality. At the same time, many governments see the value or the need to provide certain extra incentives and guarantees to attract foreign investment in a competitive market for that investment. The balance between these interests is a delicate one and may evolve over time.

Increasing complexity of investment obligations towards foreign investors

Different levels of investment protection and liberalisation in Kazakhstan's various investment treaties also raise policy issues. When countries enter into bilateral and multilateral investment agreements, this may lead to layering of different investment provisions covering the same country relations. The impact of treaty reforms can be negated because covered investors can circumvent them by choosing to bring a claim based on a more favourable treaty. Even though Kazakhstan already has an investment treaty in force with Viet Nam, there is no risk of multi-layering in this specific case: the Eurasian Economic Union-Viet Nam FTA, to which Kazakhstan is a party, provides that the investment provisions only apply between the Russian Federation and Viet Nam.[61] Issues of layering may arise, however, with respect to the EU-Kazakhstan EPCA and future investment provisions.[62] In line with the recent EU-Viet Nam FTA it can be expected, however, that any investment chapter would provide for the termination of effects of existing bilateral agreements between EU member states and Kazakhstan, ensuring that no multiple layers of investment protection exist.[63]

Dispute settlement under investment treaties

Starting in the 1990s, mechanisms for covered investors to bring claims directly against host governments – ISDS mechanisms – for alleged violations of treaty obligations have become a frequent feature of investment treaties. OECD research shows that around 96% of the global IIA stock provides access to ISDS (Pohl et al., 2012). It appears that all of the bilateral investment treaties to which Kazakhstan is a party – all signed in the 1990s or later – contain ISDS provisions. While it is difficult to establish a precise number and status of investment claims due to the confidentiality of certain ISDS proceedings (see Box 3.7), there have reportedly been 15 claims against the Kazakh government and four claims by Kazakh investors against the countries where they invested.[64]

ISDS has become controversial in a number of jurisdictions, including those that Kazakhstan has treaties with. Some of these jurisdictions are reviewing their ISDS policies and proposing new approaches, which Kazakhstan might wish to consider adopting as well.

Arbitral proceedings and recent reforms

ISDS provisions in existing treaties almost always provide for investor-state arbitration (ISA). ISA generally involves *ad hoc* arbitration tribunals selected for each case in an approach derived from international commercial arbitration (Gaukrodger and Gordon, 2012). Both the parties and arbitration institutions can be involved in the selection process. The emphasis is on finality and there are no appeals; arbitrators' decisions are subject only to very limited review.

Proponents of ISA contend that it provides a forum to settle disputes that is independent from both the host state and the investor. The importance of the parties being able to choose arbitrators has been emphasised as a core attraction of arbitration for parties because it arguably ensures that the tribunal is both unbiased and expert in international investment law (Mourre, 2010). However, ISA has been increasingly challenged in recent years. Issues raised in the debate include among other things the characteristics of a pool of investment arbitrators dominated by private lawyers, concerns about inconsistent outcomes, and alleged conflicts of interest and economic incentives among arbitrators and arbitration institutions (Gaukrodger and Gordon, 2012: 43, 58). The European Union has recently rejected ISA and developed a new approach to dispute settlement under investment treaties. It proposes to set up a permanent court and an appellate tribunal to resolve investor-state disputes (the Investment Court System [ICS]). This approach has been included in the EU-Canada CETA and the EU-Viet Nam FTA (see Box 3.6). EU Member States are parties to almost half of the approximately 3000 existing investment treaties, including over 10 with Kazakhstan, and the ICS approach has been supported in public statements by a number of EU Member states.[65]

Box 3.6. **Permanent investment courts and appellate tribunals as a replacement for ISA**

Competence over foreign direct investment was transferred from EU Member states to the EU in the 2009 Lisbon treaty. The EU development of the ICS provisions as part of its investment treaty policy follows the outcome of a 2014-15 EU public consultation on the investment provisions in the Transatlantic Trade and Investment Partnership (TTIP), extended public debates about ISDS, and input from the European Parliament and national Parliaments in Europe. The European Commission has explained the ICS as a response to "a fundamental and widespread lack of trust by the public in the fairness and impartiality of the old ISDS model" of ad hoc investment arbitration and a way to help "enshrine government's right to regulate".[66]

Box 3.6. **Permanent investment courts and appellate tribunals as a replacement for ISA** *(cont.)*

The ICS continues to allow for claims against governments by individual covered foreign investors, but seeks to address legitimacy issues associated with such claims in investment arbitration by "introducing the same elements that lead citizens to trust their domestic courts". These include judges publicly appointed in advance by governments, removal of certain perceived economic incentives and conflicts of interest among adjudicators and appointing authorities, transparency of dispute settlement, and elimination of foreign investor input into the selection of judges in individual cases. The ICS also contains innovative provisions to help investors by accelerating the treatment of claims and facilitating access to dispute settlement for SMEs. Aspects of the system that have attracted interest and commentary include its approach to the enforcement of awards, the selection of judges and appellate members, and the functioning in light of the expected flow of cases.

The EU has proposed negotiations towards a permanent multilateral International Investment Court and appellate tribunal. Canada and Viet Nam have expressed support for such work in their treaties with the EU. Questions remain about how individual treaty versions of the ICS could evolve into or be superseded by a multilateral ICS that would apply to many treaties.

ISA mechanisms in investment treaties are typically subject to only low levels of regulation (Pohl et al., 2012: 39; Gaukrodger and Gordon, 2012). Some issues are addressed by the arbitration rules, but as rules designed for commercial disputes between private parties, they may need adjustment in light of the nature of investment claims. Other issues remain unregulated if the treaties refrain from doing so. For example, in the absence of treaty provisions, ISDS is often non-transparent (see Box 3.7 on the issue of transparency).

Box 3.7. **Transparency of dispute settlement under international investment agreements**

The lack of transparency of arbitral proceedings features high on the list of concerns regarding the IIA regime. Investor-state proceedings usually involve issues of public interest: it is at stake when the investor challenges regulatory measures ostensibly or actually taken in the public interest, or when the host state, i.e. the taxpayer, has to pay compensation. Transparency of arbitral proceedings is an important means to shed light on these questions and how they are dealt with. In general, the argument in favour of confidentiality is less convincing than in private proceedings, between two companies, for example.

Box 3.7. **Transparency of dispute settlement under international investment agreements** *(cont.)*

Beyond regulations in IIAs, regulations on transparency are sometimes provided by arbitration rules. More important consequences on the transparency of arbitral proceedings are to be expected from the UNCITRAL Rules on Transparency in Treaty-based Investor-State Arbitration, which came into effect in 2014. Under the Rules, basic information about the dispute has to be made public through UNCITRAL's Transparency Registry; written submissions by the disputing parties, non-disputing parties and third parties have to be made publicly available; the oral hearings are open to the public and transcripts of those hearings have to be made publicly available; finally, all orders, decisions and awards are made publicly available. The requirements are subject to certain requirements regarding confidential and protected information.

In principle, the Rules apply to any UNCITRAL arbitration under an IIA that was concluded on or after 1 April 2014. (This is not the case when contracting parties to the IIA exclude the application of the Rules; or when the IIA allows excluding the application and both disputing parties agree to do so). For IIAs concluded before that date, the Rules only apply if the disputing parties agree to the application, or the contracting parties provide for their application on or after 1 April 2014. By signing and ratifying the UN Convention on Transparency in Treaty-Based Investor-State Arbitration, open for signature since 17 March 2015, a country makes the Rules applicable to its IIAs concluded before 1 April 2014.

The available data suggest that Kazakh IIAs also provide only a low level of regulation of ISA.[67] For example, few Kazakh agreements specify any time limits for claims against the government.[68] Covered investors can also frequently influence the choice of appointing authority for arbitrators through their power to choose between different arbitration rules for their claim. Kazakhstan has made efforts in several treaties to curtail investor influence by giving the International Court of Justice (ICJ) a central role in the appointment process.[69] The language of the provisions, however, does not appear to clearly specify in which cases the ICJ acts as the appointing authority. Many other recent treaties eliminate this power for investors completely by providing for a single appointing authority regardless of the arbitration rules selected.[70] Kazakh treaties also typically do not expressly address the issue of shareholder claims for reflective loss which have greatly expanded the scope for investor claims (see Box 3.8). The treatment of many issues is in effect borrowed from commercial arbitration practice and may not be adapted to the investor-state dispute context.

Box 3.8. **Claims for reflective loss**

Many ISDS claims today are by foreign shareholders for reflective loss. (Shareholders' reflective loss is incurred as a result of injury to "their" company, typically a loss in value of the shares; it is generally contrasted with direct injury to shareholder rights, such as interference with shareholder voting rights.) Kazakh IIAs generally do not expressly address the issue of claims by shareholders' reflective loss. Advanced systems of corporate law generally prohibit individual shareholder claims for reflective loss. Only the directly-injured company can recover the loss.

In ISDS claims brought under typical bilateral investment treaties that – like the Kazakh treaties – do not expressly address the issue of reflective loss, arbitrators have consistently permitted shareholders to claim for reflective loss. Outcomes thus differ under advanced systems of corporate law and typical bilateral investment treaties (Gaukrodger, 2013: 32-51).

Analysis and discussion of reflective loss at the OECD have demonstrated that the availability of reflective loss claims raises a broad range of policy issues for governments.[71] These include the risk of multiple claims and inconsistent decisions arising out of a single injury, exposure to double recovery, the impact on predictability, hindering settlement, facilitating treaty shopping by investors, and upsetting the hierarchy of claims against corporate assets under corporate law so that a claimant gets better treatment than under normal legal principles.[72] To date, no strong arguments have been identified to explain the different approach taken in investment treaties as opposed to advanced corporate law. It is widely recognised by governments that the issue merits further attention.[73] Under NAFTA-style agreements, some governments like the United States have consistently opposed the availability of such claims and the applicable law is subject to some uncertainty. TPP generally follows the NAFTA approach in this area. Kazakhstan could consider addressing the issue of reflective loss expressly, for example through clarifications to treaty language.

Enforcement of awards

The international community has developed specific institutions and rules to enforce arbitration awards. As noted above in the section on commercial arbitration, Kazakhstan has adhered to the New York Convention (see above). It is also a contracting state to the 1965 Convention on the Settlement of Investment Disputes between States and Nationals of Other States (ICSID Convention) which has over 150 state parties.

The ICSID Convention addresses both the arbitral proceedings and the enforcement of awards rendered under these proceedings. The recognition and enforcement of ICSID awards is governed by the ICSID Convention itself rather than the New York Convention. The ICSID regime is thus more

self-contained in this respect. In particular, ICSID awards cannot be reviewed by national courts of the country in which their enforcement is sought. In contrast, the New York Convention permits national courts to refuse the enforcement of awards for, inter alia, reasons of public policy.

ISDS claims under Kazakhstan's investment treaties

Out of the 15 investor claims against Kazakhstan, 4 were decided in favour of the state, 4 in favour of the investor (with damages ranging from USD 6 to 497 million), one case was settled (it is unknown whether a settlement payment was made), and 5 cases are still pending. Table 3.1 provides an overview of the cases brought against Kazakhstan and Table 3.2 an overview of the claims by Kazakh investors abroad. These cases suggest that ISDS mechanisms are actively, and successfully, invoked to challenge government conduct in Kazakhstan and therefore play an important role for the country's legal framework for investment. Moreover, it is important to bear in mind that even when treaties are not formally invoked in arbitral proceedings, they can be used by covered investors in their dealings with the government: any settlement negotiation, for example, will take place against the background of the investor's right to invoke the treaty protection before an arbitral tribunal, thereby potentially strengthening its bargaining leverage.

Table 3.1. **Cases against Kazakhstan**

No.	Year of initiation	Case name	IIA	Outcome of original proceedings	Home State of investor
1	1996	Biedermann International, Inc. v. The Republic of Kazakhstan and The Association for Social and Economic Development of Western Kazakhstan "Intercaspian" (SCC Case No. 97/1996)	Kazakhstan-United States IIA (1992)	Decided in favour of investor	United States
2	2001	AIG Capital Partners, Inc. and CJSC Tema Real Estate Company v. Republic of Kazakhstan (ICSID Case No. ARB/01/6)	Kazakhstan-United States IIA (1992)	Decided in favour of investor	United States
3	2001	CCL Oil v. Republic of Kazakhstan (SCC Case No. 122/2001)	Kazakhstan-United States IIA (1992)	Decided in favour of State	United States
4	2005	Rumeli Telekom A.S. and Telsim Mobil Telekomunikasyon Hizmetleri A.S. v. Republic of Kazakhstan (ICSID Case No. ARB/05/16)	Kazakhstan-Turkey BIT (1992)	Decided in favour of investor	Turkey

Table 3.1. **Cases against Kazakhstan** *(cont.)*

No.	Year of initiation	Case name	IIA	Outcome of original proceedings	Home State of investor
5	2007	Liman Caspian Oil BV and NCL Dutch Investment BV v. Republic of Kazakhstan (ICSID Case No. ARB/07/14)	Energy Charter Treaty	Decided in favour of State	Netherlands
6	2008	Caratube International Oil Company LLP v. Republic of Kazakhstan (I) (ICSID Case No. ARB/08/12)	Kazakhstan-United States IIA (1992)	Decided in favour of State	United States
7	2009	KT Asia Investment Group B.V. v. Republic of Kazakhstan (ICSID Case No. ARB/09/8)	Kazakhstan-Netherlands IIA (2002)	Decided in favour of State	Netherlands
8	2010	AES Corporation and Tau Power B.V. v. Republic of Kazakhstan (ICSID Case No. ARB/10/16)	Energy Charter Treaty; Kazakhstan-United States IIA (1992)	Decided in favour of neither party (liability found but no damages awarded)	United States of America Netherlands
9	2010	Anatolie and Gabriel Stati, Ascom Group S.A., Terra Raf Trans Traiding Ltd v. Republic of Kazakhstan (SCC Case No. Case No. 116/2010)	Energy Charter Treaty	Decided in favour of investor	Moldova, Republic of Romania Gibraltar
10	2011	Türkiye Petrolleri Anonim Ortaklığı v. Republic of Kazakhstan (ICSID Case No. ARB/11/2)	Kazakhstan-Turkey IIA (1992); Energy Charter Treaty	Settled	Turkey
11	2013	Caratube International Oil Company LLP and Devincci Salah Hourani v. Republic of Kazakhstan (II) (ICSID Case No. ARB/13/13)	Kazakhstan-United States IIA (1992)	Pending	United States of America
12	2013	World Wide Minerals v. Republic of Kazakhstan	Canada-Russian Federation IIA (1989)	Pending	Canada
13	2015	Aktau Petrol Ticaret A.S. and Som Petrol Ticaret A.S. v. Republic of Kazakhstan (ICSID Case No. ARB/15/8)	Kazakhstan-Turkey IIA (1992)	Pending	Turkey
14	2015	Devincci Salah Hourani and Issam Salah Hourani v. Republic of Kazakhstan (ICSID Case No. ARB/15/13)	Kazakhstan-United Kingdom IIA (1995) Kazakhstan-United States IIA (1992)	Pending	United Kingdom United States of America
15	2016	Kazakhstan Goldfields Corporation{p1}UNCITRAL	Canada-Russian Federation IIA (1989)	Pending	Canada

Source: Adapted from UNCTAD's ISDS navigator and publicly available information.

Table 3.2. **Cases by Kazakh investors abroad**

No.	Year of initiation	Case name	IIA	Outcome of original proceedings	Respondent State
1	2009	BTA Bank JSC v. Kyrgyz Republic	Kazakhstan-Kyrgyzstan IIA (1999)	Pending	Kyrgyzstan
2	2013	Consolidated Exploration Holdings Ltd. and others v. Kyrgyz Republic (ICSID Case No. ARB(AF)/13/1)	Kazakhstan-United States IIA (1992)	Settled	Kazakhstan Seychelles Denmark
3	2013	Vladislav Kim and others v. Republic of Uzbekistan (ICSID Case No. ARB/13/6)	Kazakhstan-Uzbekistan IIA (1997)	Pending	Uzbekistan
4	2013	OKKV (OKKB) and others v. Kyrgyz Republic	CIS Investor Rights Convention (1997)	Decided in favour of investor	Kyrgyzstan

Source: Adapted from UNCTAD's ISDS Navigator and publicly available information.

Decisions about review and possible renegotiation of existing investment treaties should take account of their temporal validity

The analysis of the investment treaties suggests that Kazakhstan might wish to consider reviewing its existing agreements to ensure that they well-reflect government intent and emerging sound practices in recent treaty policy.

Review and renegotiation of investment treaties takes time. It may be more easily conducted without the time pressure of either an imminent tacit renewal for an extended period or its denunciation with the attendant publicity. Kazakhstan should accordingly monitor the temporal validity of its treaties in order to allow it sufficient time to approach treaty partners where appropriate. Kazakhstan's treaties have varying duration and different mechanisms for renewal and termination. Bilateral investment treaties generally contain, in the final provisions, the definition of an initial validity period; at the end of this period, treaties are often extended tacitly either for an indefinite period or for another fixed term. Denunciation is possible at certain points in time, but requires advance notice. Most treaties define an additional period during which the treaty has effect for existing investments following termination (Pohl, 2013).

Table 3.3 shows for each of Kazakhstan's treaties the dates of signature and entry into force and key characteristics of their temporal validity (fixed term validity or open-ended validity; indefinite extension or renewal for fixed terms). Treaties that renew for fixed terms require more monitoring, as they limit the possibilities to update or unilaterally end the agreement. For all treaties, Table 3.3 also shows additional information such as the approximate date when the current period to give notice of denunciation ends (i.e. the last notice date before tacit renewal) and the approximate first date when the treaty could cease to be in force.[74]

The temporal validity of Kazakhstan's treaties can also inform discussions on possible joint interpretations of treaty provisions with treaty partners. Joint

Table 3.3. **Kazakhstan's investment treaties and their temporal validity**

Investment treaty	Date of signature	Date of entry into force	Definition of temporal validity	Last notice date before tacit renewal (approximate date)	Treaty will be in force at least until (approximate date)
Bilateral treaties					
Afghanistan-Kazakhstan BIT (2012)	27-09-2012		*		
Armenia-Kazakhstan BIT (2006)	06-11-2006		*		
Austria-Kazakhstan BIT (2010)	12-01-2010	21-12-2012	Indefinite extension	21-12-2022	22-12-2023
Azerbaijan-Kazakhstan BIT (1996)	16-09-1996	30-04-1998	Indefinite extension	20-10-2016	21-10-2017
Belgium/Luxembourg-Kazakhstan BIT (1998)	16-04-1998	06-02-2001	Renewal for fixed terms	07-08-2020	06-02-2021
Bulgaria-Kazakhstan BIT (1999)	15-09-1999	20-08-2001	Renewal for fixed terms	19-08-2020	20-08-2021
China-Kazakhstan BIT (1992)	10-08-1992	18-08-1994	Indefinite extension	20-10-2016	21-10-2017
Czech Republic-Kazakhstan BIT (1996)	08-10-1996	02-04-1998	Indefinite extension	20-10-2016	21-10-2017
Egypt-Kazakhstan BIT (1993)	14-02-1993	08-08-1996	Indefinite extension	20-10-2016	21-10-2017
Estonia-Kazakhstan BIT (2011)	20-04-2011	26-08-2014	*		
Finland-Kazakhstan BIT (1992)	29-09-1992	14-02-1998	Indefinite extension	No action required	Expired or otherwise terminated
Finland-Kazakhstan BIT (2007)	09-01-2007	01-05-2008	Indefinite extension	01-05-2018	02-05-2019
France-Kazakhstan BIT (1998)	03-02-1998	21-08-2000	Renewal for fixed terms	21-08-2019	21-08-2020
FYROM-Kazakhstan BIT (2012)	02-07-2012	21-05-2016	Renewal for fixed term	20-05-2025	21-05-2026
Georgia-Kazakhstan BIT (1996)	17-09-1996	24-04-1998	*		
Germany-Kazakhstan BIT (1992)	22-09-1992	10-05-1995	Indefinite extension	20-10-2016	21-10-2017
Greece-Kazakhstan BIT (2002)	26-06-2002		Renewal for fixed terms		
Hungary-Kazakhstan BIT (1994)	07-12-1994	03-03-1996	**		
India-Kazakhstan BIT (1996)	09-12-1996	26-07-2001	Indefinite extension	20-10-2016	21-10-2017
Iran-Kazakhstan BIT (1996)	16-01-1996	03-04-1999	*		
Israel-Kazakhstan BIT (1995)	27-11-1995	19-02-1997	Indefinite extension		
Italy-Kazakhstan BIT (1994)	22-09-1994	18-06-1996	Definite term	No action required	Expired or otherwise terminated
Japan-Kazakhstan BIT (2015)	23-10-2014	25-10-2015	Indefinite extension	06-04-2023	06-04-2024
Jordan-Kazakhstan BIT (2006)	29-11-2006	01-07-2008	*		
Korea-Kazakhstan BIT (1996)	20-03-1996	26-12-1996	Indefinite extension	20-10-2016	21-04-2017
Kuwait-Kazakhstan BIT (1997)	31-08-1997	01-05-2000	*		
Kyrgyzstan-Kazakhstan BIT (1997)	08-04-1997	01-06-2005	*		
Latvia-Kazakhstan BIT (2004)	08-10-2004		*		
Lithuania-Kazakhstan BIT (1994)	15-09-1994	25-05-1995	Indefinite extension	20-10-2016	19-01-2017
Malaysia-Kazakhstan BIT (1996)	27-05-1996	03-08-1997	Indefinite extension	20-10-2016	21-10-2017
Mongolia-Kazakhstan BIT (1994)	02-12-1994	13-05-1995	Renewal for fixed	12-05-2019	12-05-2020
Netherlands-Kazakhstan BIT (2002)	27-10-2002	01-08-2007	Renewal for fixed terms	29-01-2022	31-07-2022
Pakistan-Kazakhstan BIT (2003)	08-12-2003	01-10-2009	The agreement is valid for a period 10 years. It may be extended for an indefinite period by mutual consent.	01-10-2019	01-04-2020

Table 3.3. **Kazakhstan's investment treaties and their temporal validity** *(cont.)*

Investment treaty	Date of signature	Date of entry into force	Definition of temporal validity	Last notice date before tacit renewal (approximate date)	Treaty will be in force at least until (approximate date)
Poland-Kazakhstan BIT (1994)	21-09-1994	25-05-1995	*		
Qatar-Kazakhstan BIT (2008)	04-03-2008		*		
Romania-Kazakhstan BIT (1996)	25-04-1996	05-04-1997		No action required	Expired or otherwise terminated
Romania-Kazakhstan BIT (2010)	02-03-2010	02-07-2013	Renewal for fixed terms	01-07-2022	02-07-2023
Russian Federation-Kazakhstan BIT (1998)	06-07-1998	11-02-2000	Indefinite extension	20-10-2016	21-10-2017
Serbia-Kazakhstan BIT (2010)	07-10-2010	07-12-2015	Indefinite extension	06-12-2025	07-12-2026
Slovakia-Kazakhstan BIT (2007)	21-11-2007	29-06-2016	*		
Spain-Kazakhstan BIT (1994)	23-03-1994	22-06-1995	Renewal for fixed terms	20-12-2016	21-06-2017
Sweden-Kazakhstan BIT (2004)	25-10-2004	01-08-2006	Indefinite extension	31-07-2021	01-08-2022
Switzerland-Kazakhstan BIT (1994)	12-05-1994	13-05-1998	Renewal for fixed terms	11-11-2017	13-05-2018
Tajikistan-Kazakhstan BIT (1999)	17-12-1999	20-11-2001	*		
Turkey-Kazakhstan BIT (1992)	01-05-1992	10-08-1995	Indefinite extension	20-10-2016	21-10-2017
Ukraine-Kazakhstan BIT (1994)	17-09-1994	04-08-1995	**		
United Kingdom-Kazakhstan BIT (1995)	23-11-1995	09-01-1997	Indefinite extension	20-10-2016	21-10-2017
United States-Kazakhstan BIT (1992)	19-05-1992	12-01-1994	Indefinite extension	20-10-2016	21-10-2017
Uzbekistan-Kazakhstan BIT (1997)	02-06-1997	08-09-1997	*		
Viet Nam-Kazakhstan BIT (2009)	15-09-2009	07-04-2014	*		

* No official treaty text found: dates could not be calculated.
** Uncertain: dates could not be calculated.

interpretations can be issued at any time and can be a simpler and faster device than renegotiation to address some aspects of treaty policy providing that the existing treaty text allows sufficient scope to achieve the jointly-desired interpretation. This may often be the case in older treaties with vague provisions. Discussions and exchanges of views with treaty partners about proposed joint interpretations in advance of treaty renewal dates can also help inform future negotiations and decisions about treaties.

Policy recommendations

Adequate levels of investment protection and effective mechanisms to enforce investor rights and government obligations are an important pillar for an attractive investment climate in Kazakhstan. Efforts to achieve an attractive investment climate need to balance investor protection and the government's right to regulate. Over the last years, Kazakhstan has continued to work on improving the policy and legal framework for the balancing of

investor protection and the power to regulate. At the same time, continuing legitimate concerns by investors and other stakeholders need to be taken seriously. The Kazakh authorities might wish to consider the following recommendations to further improve the country's policy framework for investment.

- *Bear in mind that regulatory change imposes costs*. The analysis of Kazakhstan's legal framework reveals that the rules applicable to investors have changed considerably over the last years. While reforms are necessary and valuable in many areas, it is important to consider that repeated changes can cause uncertainties and compliance costs.
- *Consider policy rationale for offering different levels of protection to different groups of investors*. While there can be value or the need to provide certain extra incentives to attract specific investors, e.g. foreign investors or investors in certain sectors and projects, Kazakhstan should seek to guarantee a sound investment climate for all investors and consider whether distortions to efficient investment decisions may occur.
- *Continue efforts to improve functioning of the court system*. Recent improvements in indexes and surveys suggest that Kazakhstan is on the right way towards enhancing the quality of its court system. These efforts should be further strengthened.
- *Ensure that timely preparation of new rules and regulations does not come at expense of their consistency and clarity*.
- *Focus on establishing a regulatory environment which enhances investor confidence*. Stability assurances should be used carefully because they directly constrain the government's future ability to regulate. They should be seen as a useful tool to increase investor confidence until an improved overall legal framework ensures adequate predictability and protection.
- *Specify treaty language to ensure that treaties accurately reflect government intent*. Treaty provisions in the vast majority of Kazakhstan's treaties are relatively broad, leaving arbitrators a lot of leeway in determining the actual scope of protection they provide. The absence of clear government intent for many of these provisions may pose significant challenges for the government in the quest for balance between investor protection and its own power to regulate.
- *Review existing investment treaties*. Kazakhstan has stated that it is currently reviewing its investment treaty policy. As part of this initiative, the authorities should seek to ensure improved treaty design is also reflected in Kazakhstan's network of existing treaties.
- *Manage liability risks under investment treaties actively*. The authorities should seek to ensure that different government agencies and officials are aware of

treaty policy and the obligations it entails. Efforts to improve the management of risks could include training programs for government officials and the creation of dispute prevention and management mechanisms.

Notes

1. Article 6(2), Constitution.
2. Article 14, Constitution.
3. The analysis of the Entrepreneurial Code and other laws and regulations has been developed on the basis of unofficial English translations of the text. The terms used in the analysis might therefore not necessarily reflect the actual meaning of the official text or government intent more broadly.
4. See for example article 7, Entrepreneurial Code, on the inviolability of property.
5. Article 279(1), Entrepreneurial Code. According to information provided by the Kazakh authorities, the compensation paid in case of nationalisation shall include the loss of expected gains, whereas the payment in case of requisition only corresponds to the fair market value, to be determined pursuant to the provisions of the Law on Evaluation Activity from 30 November 2000.
6. Under article 253, Civil Code, requisition is defined as: "In cases of natural calamities, accidents, epizootic epidemics, and under any other circumstances which have an extraordinary nature, property may be requisitioned in the interests of the society upon the resolution of the state bodies from an owner in accordance with the procedure and on the conditions established by legislative acts, with the payment to him of the value of the property (requisition)."
7. Article 279(2)-(4), Entrepreneurial Code.
8. According to information provided by the Kazakh authorities, "conditions similar to expropriation through […] government measures [are] impossible", suggesting that indirect expropriation may be covered by the expropriation provisions as well.
9. Similar provisions are also included in article 9(5), Civil Code, applicable to citizens and legal entities generally.
10. Article 276(1)-(2), Entrepreneurial Code. Investors must be accorded "full and unconditional" protection of the rights and interests provided by the Constitution, the Code and other normative legal Article 274, Entrepreneurial Code: "Major investors" are defined as those investing not less than two million times the monthly calculation index, which was set at 2 121 (two thousand one hundred twenty-one) tenge on 1 January 2016.
11. Articles 283 and 289, Entrepreneurial Code, in particular acts, and international treaties ratified by Kazakhstan.
12. See Articles 283 and 289, Entrepreneurial Code, in particular.
13. According to information provided by the Kazakh authorities, the different categories exist to support development of priority economic sectors, such as food processing, chemicals, and manufacturing.
14. See OECD Policy Framework for Investment, 2015: 26.
15. See website of the World Intellectual Property Organisation for the full list of agreements: *www.wipo.int/wipolex/en/profile.jsp?code=KZ*.

16. These include the Law No. 456 of 26 July 1999 on Trademarks, Service Marks and Appellations of Origin (as amended up to Law of the Republic of Kazakhstan No. 378-V of 31 October 2015) (2016); the law on Patents of the Republic of Kazakhstan No. 427-I of 16 July 1999 (as amended up to Law of the Republic of Kazakhstan No. 378-V of 31 October 2015) (2016); the law of the Republic of Kazakhstan No. 422-I of 13 July 1999, on the Protection of Selection Achievements (as amended up to Law of the Republic of Kazakhstan No. 378-V of 31 October 2015) (2016); the Law of the Republic of Kazakhstan No. 6-I of 10 June 1996, on Copyright and Related Rights (as amended up to Law of the Republic of Kazakhstan No. 419-V of 24 November 2015) (2016); the Law of the Republic of Kazakhstan No. 300-V of 7 April 2015, on Amendments and Addenda to Some Legislative Acts of Kazakhstan on the Issues of Legal Regulation of Intellectual Property (2015); and the Law No. 217-II of 29 June 2001, on Legal Protection of Layout Design of Integrated Microcircuits (as amended up to Law of the Republic of Kazakhstan No. 382-V of 31 October 2015) (2015).
17. These areas are addressed in more detail in OECD (2016a), *Boosting Kazakhstan's National Intellectual Property System for Development and Innovation*.
18. See web-site of the Prime Minister of Kazakhstan: "Kazakhstan investment climate needs clear and transparent rules", 12 March 2014, *https://primeminister.kz/news/show/21/investitsionnyj-klimat-rk-nuzhny-chetkie-i-prozrachnye-pravila-igry-/12-03-2014?lang=en*.
19. Peru for example offers a legal stability agreement to local and foreigners who have invested more than USD 10 million in the mining or hydrocarbon sectors, or USD 5 million in any other financial activities. The legal stability agreement only offers "Stability of non-discrimination rights, Tax Income Regime applicable to investors, free disposal of currencies and rights to make remittances of gains, profit and royalties, applicable to foreign capitals". The validity of the Agreement is 10 years, unless the underlying concession contract has a longer validity period. See the Peruvian investment promotion agency's website. Similarly, Guinea's amended mining code from 2013 provides that stabilisation commitments regarding the tax regime are limited to 15 years and specifically excludes certain aspects of the tax regime that cannot be stabilised at all. While the code thus sets general rules for stabilisation, the mining concessions will contain more specific provisions (see article 182 of the Mining Code Guinea (2013)).
20. According to information provided by the Kazakh authorities, stability shall ensure the "inalterability of terms and conditions of the contract".
21. Defined in article 279, Tax Code.
22. Article 276(3), Entrepreneurial Code.
23. See for example AEQUITAS Law Firm, Briefing, 28 December 2015: *http://aequitas.kz/upload/files/Information%20Memorandum_Entrepreneurial%20Code%20of%20the%20Republic%20of%20Kazakhstan.pdf*.
24. The definition of "national security" under article 4 of the National Security Law from 2012 lists "environmental security" as of it its components.
25. Article 289, Entrepreneurial Code.
26. Article 284, Entrepreneurial Code.
27. See Article 9, draft Code "On Subsurface and Subsurface Use" from February 2016.
28. See for example the agreement signed between Kazakhstan and Japan (Article 7, see Table 3.3).

29. See Section VI, draft Code "On Subsurface and Subsurface Use" from February 2016.
30. The OECD Conference on Investment Treaties discussed the search for improved balance through new institutions or improved rules for dispute settlement including the new Investment Court System developed by the European Union. A summary is available here: *www.oecd.org/daf/inv/investment-policy/OECD-investment-treaties-2016-summary.pdf*.
31. Article 301, Entrepreneurial Code. The CPC is available at: *http://adilet.zan.kz/kaz/docs/K1500000377*.
32. Article 303, with further details in articles 302-305, Entrepreneurial Code
33. Article 296(1) and (2), Entrepreneurial Code.
34. Article 296(3), Entrepreneurial Code.
35. Doing Business measures the time and cost for resolving a standardised commercial dispute through a local first-instance court. It also evaluates whether a series of good practices that promote quality and efficiency in the court system has been adopted (World Bank, 2016: 84). It is worth noting that changes in investment climate captured by World Bank's Doing Business do not necessarily reflect the quality, transparency, and predictability of investment-related policies, laws and regulations, nor the consistency in their implementation. The reforms focused primarily on improving such rankings may hence miss the mark in terms of improving factors that truly matter for investors.
36. See article 296, Entrepreneurial Code.
37. Article 274, Entrepreneurial Code: "Major investors" are defined as those investing not less than two million times the monthly calculation index, which was set at 2121 tenge (around EUR 11 million) on 1 January 2016 (Ernst & Young, 2016).
38. For additional reports, see CIS Arbitration Forum, "New ADR Regulations enacted in Kazakhstan", 26 January 2016, *www.cisarbitration.com/2016/01/26/new-adr-regulations-enacted-in-kazakhstan/*.
39. Chapter 1, Arbitration Law.
40. Chapter 3, Arbitration Law.
41. Article 8, Arbitration Law.
42. Article I(1), New York Convention.
43. Articles 11 and 12, Arbitration Law.
44. See the DIFC's website for further information: *www.difc.ae/about*.
45. AIFC law, Article 2.
46. The term IIA covers both stand-alone treaties and investment chapters in broader free trade agreements.
47. The review analysed selected treaties, located on different databases (OECD, UNCTAD).
48. See article III, United States-Kazakhstan IIA (1992) or more recently article 12, Japan-Kazakhstan IIA (2014).
49. See Trans-Pacific Partnership agreement, signed in February 2016; or the investment chapter proposal of the European Union, presented in 2015, and recent practice in ASEAN.

50. The numbers are based on the UNCTAD ISDS database (available at: investment policyhub.unctad.org/ISDS/), which refers to 668 cases. Data on alleged breaches is available for 425 of them.

51. See article 8.31, Eurasian Economic Union-Viet Nam FTA, and the specification in paragraph 2; the investment chapter, which contains more specific language, only applies between the Russian Federation and Viet Nam, see article 8.2(1).

52. See recent ASEAN-practice, TPP, or the EU-approach.

53. Article 6, Japan-Kazakhstan IIA (2014).

54. Article 8.7(4), CETA (2016).

55. See for example US Schedule to Annex II list of non-conforming sectors, p. II-US-11 (excluding from MFN any "bilateral or multilateral international agreement in force or signed prior to the date of entry into force").

56. Article 18, Japan-Kazakhstan IIA (2014): "Notwithstanding any other provisions in this Agreement other than the provisions of Article 13 of this Agreement, each Contracting Party may take any measure: (a) which it considers necessary for the protection of its essential security interests; i) taken in time of war, or armed conflict, or other emergency in that Contracting Party or in international relations; or ii) relating to the implementation of national policies or international agreements respecting the non-proliferation of weapons; or (b) in pursuance of its obligations under the United Nations Charter for the maintenance of international peace and security. 2. In cases where a Contracting Party takes any measure, pursuant to paragraph 1above, that does not conform with the obligations of the provisions of this Agreement other than the provisions of Article 13 of this Agreement, that Contracting Party shall not use such measure as a means of avoiding its obligations."

57. Article 20, Japan-Kazakhstan IIA (2014).

58. See e.g. article 1(1), Egypt-Kazakhstan IIA (1993).

59. Article 24, Japan-Kazakhstan IIA (2014). Similar clauses have emerged more broadly in more recent treaty practice: see articles 4 and 5, Austria-Kazakhstan IIA (2010).

60. United States Government Accountability Office (2009), "Four Free Trade Agreements GAO Have Reviewed Have Resulted in Commercial Benefits, but Challenges on Labor and Environment Remain", available at: *www.gao.gov/assets/300/292204.pdf*. In 2014, the US has brought a claim against Guatemala for an alleged breach of obligations regarding labour rights under CAFTA-DR.

61. See Human Rights Watch, Q&A: The Trans-Pacific Partnership, 12 January 2016, available at: *www.hrw.org/news/2016/01/12/qa-trans-pacific-partnership*.

62. See article 8.2(1).

63. Article 57 of the EPCA provides that the Parties shall review the legal framework for investment and consider the inclusion of investment protection provisions.

64. See investment chapter, article 20, EU-Viet Nam FTA.

65. 15 according to UNCTAD plus one in 2016 according to IAReporter.

66. See for example statements by the German Ministry of the Economy (*www.bmwi.de/DE/Themen/Aussenwirtschaft/investitionsschutz.html*) and the French government (*www.diplomatie.gouv.fr/en/french-foreign-policy/economic-diplomacy-foreign-trade/events/article/expectations-of-france-and-germany-regarding-the-transatlantic-trade-and*).

67. Malmström, C. (16 September 2015), "Proposing an Investment Court System", *https://ec.europa.eu/commission/2014-2019/malmstrom/blog/proposing-investment-court-system_en*.
68. Assessment based on the OECD investment treaty data base and the analysis of selected treaties.
69. Article 17(9), Japan-Kazakhstan IIA (2014).
70. See for example article 13, Austria-Kazakhstan IIA (2010), which allows the investor to choose between different fora, including ICSID, ICC, and arbitration under the UNCITRAL Rules. The treaty does not provide for a single appointing authority but specifies that, in the absence of any relevant arrangement, either party may invite the President of the International Court of Justice to make the necessary appointments. Similar provisions are also found in other Kazakh IIAs, e.g. with Finland or the Netherlands.
71. See for example article 9.22(3), TPP.
72. Cf. Eilís Ferran, Summary of FOI Roundtable 19, pp. 18-19. In addition to shareholders, creditors can also suffer reflective loss and may be able to file claims for such loss under some treaties. Summary available at: *www.oecd.org/investment/investment-policy/19thFOIroundtableSummary.pdf*.
73. Summary of FOI Roundtable 19, pp. 18-19.
74. Summary of FOI Roundtable 19, pp. 18-19.
75. This information is provided as a matter of general analysis and should not be relied on with regard to individual treaties. Recourse should be had to the precise treaty text in each case. The dates do not take into consideration the possibility of an agreement by the treaty partners to amend and/or terminate the treaty. The reference date for the calculation is 20 October 2016. The calculation is also approximate due to the different length of months and years.

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Chapter 4

Kazakhstan's tax policy

Kazakhstan's ambition of joining the top 30 most developed countries by 2050 will largely depend on its ability to create an investment-stimulating business environment, putting in place the ingredients necessary for the private sector expansion, including, more importantly than ever, diversification of investment into non-extractive industries. Kazakhstan's tax regime is one of the key policy instruments that can either encourage or discourage investment. Kazakhstan has been offering generous tax incentives to make the investment climate more attractive. Despite on-going efforts aimed at rationalising investment incentives, the taxation regime remains somewhat complex, the country applying tax reliefs that vary depending on the type of investment, its location or activity. There is uncertainty as to whether they meet their intended objectives. In general, there has been inadequate analysis to assess their effectiveness. Establishing mechanisms to regularly evaluate the costs and benefits of tax incentives would help assess them against their intended policy objectives as well as the associated fiscal cost.

Kazakhstan's tax framework is another policy instrument that can either encourage or discourage investment. It also an important component of the *Declaration on International Investment*, which includes the Instrument on *International Investment Incentives and Disincentives*. The latter encourages Adherents to ensure that incentives as well as disincentives are as transparent as possible so that their scale and purpose may be easily determined. The Instrument also provides for consultations and review procedures among Adherents to facilitate international co-operation in this area. Kazakhstan has constantly improved its tax framework and the country now relies on a well-developed system that has been adjusted over time depending on specific economic and social circumstances. To attract investors, the country has offered tax and other non-tax incentives to make the FDI climate more attractive. While the merits of tax investment incentives will depend upon the specific objectives of the incentives, the type and mix of incentives provided and the design of the incentives, there is a danger that the benefits of such incentives are likely to be limited, and could contribute to a harmful 'race to the bottom' among countries competing to attract investors. This is especially the case where tax investment incentives have been introduced without a comprehensive assessment of their costs and benefits. Most recent reforms have seen efforts by the authorities to rationalise their investment tax incentives.

Kazakhstan's tax framework

The taxation regime in Kazakhstan is regulated by the Tax Code, which is relatively new (having been rewritten in 2009). Kazakhstan was the first of the CIS countries to adopt a comprehensive Tax Code in 1995. The 1995 Tax Code combined all existing legal framework for taxation except for customs duties, contributions for social insurance, and state duties. There were almost 50 different taxes before the tax reform and only about a dozen after the reform (Witt and McLure, 2001). The 1995 Code provided the basis of a modern tax system in Kazakhstan.

Since then, the tax system has changed several times, dynamically responding to the changing priorities of the government. One set of substantive changes was introduced through the adoption of the new Tax Code in December 2008.[75] Designed during the era of elevated commodity and oil prices, the Code aimed at diversifying the economy away from the natural resource extraction. To achieve this, the Code of 2008 attempted to shift the tax burden to the

Subsurface users by raising taxes on the sector, while significantly reducing the statutory corporate tax rate and simplifying the tax system outside the subsurface production. At the same time, the Code eliminated subsurface contract stability provisions from many subsurface use contracts.[1] Table 4.1 below presents a detailed overview of Kazakhstan's tax system in effect at the end of 2016, including the taxation of subsurface users.

Table 4.1. **Kazakhstan's tax regime**

Legal basis of taxation	**The Code of the Republic of Kazakhstan "On taxes and other obligatory payments in the budget" (the Tax Code).** Law No. 99-IV of the Republic of Kazakhstan of 10 December 2008	
Tax Residency	A company is a tax resident if • it is established under the laws of Kazakhstan, or • its place of effective management is located in Kazakhstan.	
	Tax residents are taxed on their worldwide income.	
	Non-residents are taxed only on Kazakhstan source income.	
Profit tax		
Subjects to profit tax (article 147)	Subject to tax are resident, as well as and non-resident companies that • operate through a permanent establishment, or • receive income from Kazakhstan sources that are deemed payers of profits tax.	
Tax rate	Standard rate	20%
	An additional branch profit tax applicable to after-tax profit of permanent establishments	15% (Could be reduced to 5% under an Agreement on the Avoidance of Double Taxation.)
	Producers of agricultural products, aquacultural (fishery) products, and for rural consumer co-operatives	6%
	Non-residents' income from sources in Kazakhstan	15%
Depreciation rates of fixed assets	Tax Code, Article 120, defines maximum rate of depreciation of fixed assets	
	• Buildings, structures, except for oil, gas wells and transmission equipment	10%
	• Machines and equipment, except for machines and equipment for oil and gas production, and also computers and equipment for information processing	25%
	• Computers, software and equipment for information processing	40%
	• Fixed assets not included in other groups, including oil, gas wells, transmission equipment, machines and equipment for oil and gas production	15%
	Entities implementing a priority project and not using special tax treatment apply depreciation rates in the amount of at least 50% of the maximum depreciation rates	
Losses carried forward	10 years following the year in which the loss was incurred	
Withholding Tax		
(Article 194)		
	Non-residents without a permanent establishment (PE) in Kazakhstan	
	• Dividend	15%
	• Royalty	15%
	• Capital gains	15%

Table 4.1. **Kazakhstan's tax regime** *(cont.)*

	• Income from providing services (other than insurance and international transportation services)	20%
	• Insurance premiums paid under risk insurance contracts	15%
	• Insurance premiums paid under risk re-insurance contracts	5%
	• Income from international transportation services	5%
	• Income generated by an entity registered in a country with preferential tax treatment	20%
	• Other types of income received from a resident or non-resident with a permanent establishment	20%
	Capital gains generated at a public auction on a Kazakhstan or foreign stock exchange	Exempt
	Capital gains from the sale of shares (interest) in a Kazakhstan company; dividends paid to foreign shareholders where • the Kazakhstan entity is not a subsurface user • the Kazakhstan entity has held the shares for more than 3 years • more than 50% of the value of the shares sold is not derived from the assets of Kazakhstan Subsurface users.	Exempt
Personal income tax		
Tax rate (Article 158)	Flat rate for both resident and non-resident. (Re-introduction of progressive personal income tax rates is planned.)	10%
	Dividend income of tax resident individuals from sources within and beyond Kazakhstan	5%
	Dividend income where • the legal entity is not a subsurface user • taxpayer has been a holder of the shares or participatory interest for more than 3 years • the value of the shares derived from the assets of subsurface users does not exceed 50% on the date of the dividends payment.	Exempt
Value-Added Tax (VAT)		
Subject to VAT (Chapter 8, Article 228-229) Article 236)	Taxable items are: 1) taxable turnovers; 2) taxable import. VAT is chargeable on turnovers that take place in Kazakhstan, based on the place of turnover rules. The applicability is determined based on the deemed place of supply. The rules determining the place of supply are: • Goods: ❖ The place where transportation commences if goods are transported or mailed ❖ The place where goods are transferred to the purchaser • Works and services: ❖ The place where immovable property is located for works and services ❖ The place where works and services are actually carried out for works and services related to movable property ❖ The place of business or any other activity of the customer ❖ The place of business or any other activity of the service provider.	
VAT registration	• Required for all entities with cumulative taxable revenues in excess of 30 000 - times monthly accounting index. (approximately USD 342 000) during a calendar year. • Optional for all other persons.	
Tax Rate	Standard rate	12%
	Export sales of crude oil, natural gas and gas condensate	0%

Table 4.1. **Kazakhstan's tax regime** *(cont.)*

	International transportation services (including the transportation of oil and gas via trunk pipelines)	0%
	Sales of goods on the territory of SEZs	Goods which are fully consumed during the implementation of activities on the territory of SEZs are taxed at 0%
	Imports of goods and equipment, included in the Article 255 of the Tax Code, e.g. medical devices and equipment	0%
	The list of exempt activities is specified in the Chapter 33 of the Tax Code and includes, among others, financial services, insurance services, medical services, sale and lease of land and land use rights, etc.	Exempt
Excise		
Base of excise duties (Article 279)	Importation and sale of all types of spirits, alcohol, tobacco, petrol/gasoline (excluding aviation fuel), diesel, cars, crude oil and natural gas condensate.	
Rates	Vary; see Article 280 of the Tax Code	
Property Tax		
Taxpayers (Article 394)	Resident Kazakhstan companies (except for state institutions) and non-resident companies operating in Kazakhstan through a PE or receiving income from Kazakhstan sources	
Tax base	Average annual balance-sheet value, determined on the basis of the accounting records.	
Rate (Article 398)	Standard rate	1.5%
	Individual entrepreneurs and legal persons which apply special tax regime on the basis of a simplified declaration	0.5%
	Legal entities, as defined in Article 134 of the Tax Code, except religious associations and entities whose main activity (services) is in the field of library services in accordance with Article 135 of the Tax Code	0.1%
	Legal entities specified in paragraph 1 of Article 135-1 and organizations located in the territory of FEZ that use in the implementation of activity envisaged in the FEZ territories, autonomous educational organizations	0%
Land tax		
Taxpayers (Article 373)	Payers of land tax are physical and legal persons having taxable items: 1) on the right of ownership; 2) on the right of permanent land use; 3) on the right of primary unpaid temporary land use.	
Tax rate (Articles 378-387)	The rate depends on the land's use and the quality rating set by the Government, see Chapter 54 of the Tax Code.	
Vehicle tax		
	The rate depends on the vehicle type and engine size. See Chapter 51 of the Tax Code.	
Fee emission to the environment		
	Fee emission for emissions into the environment are charged for emission into the environment in order of special environmental management The object of taxation is the actual volume of emissions into the environment within and/or in excess of the established limits of emissions into the environment of: 1) ejection of pollutants; 2) discharge of pollutants; 3) wastes disposal of production and consumption; 4) sulphur disposal produced during oil operations.	
Rates (Article 495)	Payment rates are determined based on monthly calculation index established by the Law on the national budget for the first day of the tax period subject to the provisions of paragraph 7 of Article 495 of the Tax Code.	

Table 4.1. **Kazakhstan's tax regime** *(cont.)*

Rent tax on exports		
Taxpayers	Individuals and legal entities that implement: • crude oil and raw mineral oil, except for subsurface users which exporting quantities of crude oil and gas condensate with PSAs concluded before to January 1, 2009; • the list of legal entities is established by the competent authority in the area of oil and gas, these legal entities have to implement customs procedure for export of crude oil determined by the authorized body in the area of oil and gas and previously have to be placed under customs procedure for processing outside the customs territory • coal	
Taxable items	Volumes of crude oil and refined oil products and coal traded for export	
Tax base	• The value of exported crude oil and refined oil products is based on the actually export volume of crude oil and refined oil products and world prices. • Rent tax calculation on export of coal is based on the value of exported coal calculated on the basis of coal actually sold for export.	
Tax rates	Crude oil and refined oil products	The scale is provided depending on world prices. Rates varied from 0 to 32%.
	Coal	2.1%
Anti-avoidance rules		
Transfer pricing (The transfer pricing law, Article 3)	Control of transfer pricing is carried out for the following transactions: 1) International business transactions: The export of goods from the territory of the Republic of Kazakhstan is carried out in accordance with the customs legislation of the Customs Union and (or) the Republic of Kazakhstan, also the export of goods is carried out from the territory of the Republic of Kazakhstan to the territory of another State - a member of the Customs Union The importation of goods into the territory of the Republic of Kazakhstan is carried out in accordance with the customs legislation of the Republic of Kazakhstan, also the importation of goods is carried out into the territory of the Republic of Kazakhstan from the territory of another State - a member of the Customs Union 2) Committed in the territory of the Republic of Kazakhstan is directly related to international business transactions: Realizable minerals produced by the subsoil user, which is one of the parties one of the parties has tax exemptions one of the parties has a loss on data of tax returns for the last two tax periods preceding the year of the transaction	
Thin capitalization (Article 103)	The deduction of interest is limited either by the market rate or specific debt-to-equity formula	
CFC rules	CFC rules apply to residents with at least a 10% shareholding in an entity established in non-transparent jurisdiction. Related parties are physical and legal entities with a special relationship which has an impact on the economic results of transactions between them, including if a person is large shareholder (owns10% or more percent of voting shares)	
Legislation	• Law "On taxes and other obligatory payments in the budget" (the Tax Code). • Law No. 99-IV of the Republic of Kazakhstan of 10 December 2008. • Law No. 291-IV of the Republic of Kazakhstan on Subsurface and Subsurface Use, 24 June 2010.	
	In addition to the taxes and obligatory payments stipulated by tax legislation, all subsurface users are required to pay special taxes and other obligatory payments. These include: • signature and commercial discovery bonuses • reimbursements of historical costs • mineral production tax • excess profits tax	

Table 4.1. **Kazakhstan's tax regime** *(cont.)*

Signature and commercial discovery bonuses			
	Signature bonus is a one-time fixed payment for the right acquisition to use the subsurface in the contractual territory, as well as the expansion of the contractual territory See Article 314 of the Tax Code to determine the amount. Examples: ● For oil contracts with approved reserves – 2800-fold amount of monthly calculation index established by the Law On Republican Budget ● For oil production contracts, where reserves have not been approved 3000-fold amount 2800-fold amount of monthly calculation index established by the Law On Republican Budget **Commercial discovery bonus** is a fixed payment that is payable by subsurface users when a commercial discovery is made in the contract territory. A tax base for the assessment of the commercial discovery bonus shall be the value of the volume of mineral reserves approved by the state body authorized for these purposes. The rate of the commercial discovery bonus is fixed at 0.1%		
Reimbursements of historical costs			
	The payment for compensation of historical costs is a fixed payment for reimbursement of total costs incurred by the state for geological surveys of contractual territory and exploration of field before the conclusion of the subsurface use contract. The obligation to reimburse historical costs arises from the date the confidentiality agreement is concluded between the subsurface users and authorized state body on subsurface study and usage. (See Chapter 44 of the Tax Code.)		
Excess Profit Tax (EPT)			
Legislation	The order 1330, of September 1997, established the Procedure for Determining the Internal Rate of Return for the Calculation of Excess Profits Tax. The detailed method for calculating EPT was approved by Order 41 of the Ministry of Finance of the Republic of Kazakhstan On the Taxation of Subsurface Users dated 29th December 1997 (Instruction 41).		
Tax base	The object of EPT taxation is a part of the net income determined for each individual subsurface use contract for the tax period, which exceeds 25% of the deductions determined for EPT purposes.		
Tax rate	Scale of distribution of net income for the EPT purposes, % tax deduction.	% for computation of maximum amount of net for EPT purposes	Rate (%)
	Less or equal to 25%	25	Not established
	from 25% to 30% inclusive	5	10
	from 30% up to 40% inclusive	10	20
	from 40% up to 50% inclusive	10	30
	from 50% up to 60% inclusive	10	40
	from 60% up to 70% inclusive	10	50
	More than 70%	Any excess	60
Mineral Production Tax (MPT)			
	MPT rates apply to the value of taxable volume of recovered resources contained in raw materials, where value is based on the world price. Rate depends on the type of extracted mineral raw materials.		
Tax rate	Crude oil and gas condensate	5% to 18% (see Article 336 of the Tax Code) Can be reduced by 50% in case of sale and (or) transfer of crude oil and gas condensate production in the domestic market of Kazakhstan, including in-kind payment of (MPT), the rent tax on exports, royalties and shares of Kazakhstan under production sharing recipient on behalf of the state or to use its own production needs if supplied to domestic refineries in a sale/purchase or tolling agreement.	
	Minerals	Depends on the type of mineral; e.g. rate for copper is 5.7%, gold silver, platinum, palladium – 5%, iron ore – 2.8%, uranium – 18.5% , etc. (Article 339 of the Tax Code)	

Table 4.1. **Kazakhstan's tax regime** *(cont.)*

Stability of Tax Regime	
	The Tax Code of 2008 abolished the stability of the tax regime for Subsurface use contracts other than production sharing agreements (PSA) signed with the government prior to January 1, 2009 which passed the obligatory tax inspection, and contacts signed by the President. All other subsoil users, including those with contracts concluded before 2009, are subject to taxation in accordance with the tax law that is in effect at the time when a particular tax liability arises.

Source: Ministry of Finance of the Republic of Kazakhstan, December 2016.

In recent years, there have been a number of improvements in Kazakhstan's tax framework. A number of analyses have noted that Kazakhstan's tax laws are among the most comprehensive of the former Soviet Union states (World Bank Group, 2015). Continuous improvement of the tax institutional framework has also been part of the government's reform agenda. In August 2014, the Tax and Customs administrations merged to form the new State Revenue Committee (SRC).The World Bank Group (WBG) has been providing technical assistance in respect of the integration of the two fiscal agencies, streamlining the SRC operations, and developing the SRC strategy. As reported by the WBG, good progress has been made by Kazakhstan in improving taxpayer services and reducing the burden of taxpayer compliance.

Firms have nevertheless complained about an overly bureaucratized attitude of tax officials toward businesses, where repetitive tax inspections and varied interpretations of rules are sometimes common place. In the course of the discussions the OECD Secretariat had with Kazakhstan's tax authorities, tax officials recognized that one of their main areas of concern was indeed the "differences in interpretations of legal provisions between taxpayers and the administration". In this regard, the government has a major role to play in developing guidance targeting both tax officials and investors. It is important for the tax regulations to be clearly and objectively defined and explained in order to ease compliance and to decrease unnecessary disputes between taxpayers and tax authorities. Overly complex or unpredictable rules, ambiguous criteria that leave room to subjective interpretation introduce opportunity for rent seeking on the part of investors and invite corrupt behaviour on the part of public officials. Transparent, uniform, rule-based systems, with a uniform approach and interpretation of the tax provisions, allow investors to have a clearer understanding of the tax environment they would be investing in and give them far less to fear from the lack of a level playing field.

Tax investment incentives

Empirical evidence finds that taxes matter for investment (OECD, 2015), although the efficacy of tax investment incentives will depend upon the

specific objectives of the incentives, the type and mix of incentives provided and the design of the incentives. There is also some evidence to suggest that tax incentives are likely to be more effective as a country becomes more economically developed, however, this may simply reflect the fact that more developed countries are also likely to demonstrate many of the other attributes that contribute to an attractive investment environment. Since the provision of tax incentives involves government foregoing revenue, the benefits of associated with tax incentives need to be weighed against the costs, including their revenue costs.

Tax incentives have been routinely used by Kazakhstan to attract investment in general, and foreign direct investment in particular. Tax incentives have been seen by the authorities as a way to attract investment into non-oil sectors, aiming primarily at the economic diversification away from subsurface production. With mineral prices continuously depressed, the Kazakh authorities decided in 2014 to introduce a new package of incentives aimed at attracting foreign investment into the non-oil sector, to give another boost to the economic diversification of the country. As a result, Kazakhstan's tax system remains characterised by many exemptions, particularly in the area of corporate income tax (CIT) and VAT. This incentives regime, which currently includes common incentives, available to all taxpayers, and a separate set of measures targeted at investment into government-identified priority sectors and Special Economic Zones (SEZs), is summarized in Table 4.2 below.

Table 4.2. **Investment Incentives**

General/common incentives	
Types of investment projects Article 283 of Entrepreneurial Code	Investment preferences are provided for: 1) investment projects: • exemption from customs duties and value added tax on imports • state in-kind grants 2) investment priority projects: • exemption from customs duties • state in-kind grants • tax preferences • investment subsidies 3) investment strategic projects: • tax preferences
Exemption from customs duties Article 287 of Entrepreneurial Code	• Exemption from customs duties on imported components, spare parts, and raw materials. • Exemption from customs duties on imported manufacturing equipment over the duration of the investment contract but not to exceed 5 years after the registration of the investment contract. • Exemption from customs duties on imported spare parts for equipment for up to five years are provided to legal entities of Kazakhstan depending on investment in fixed assets. • Exemption from customs duties is provided over the duration of the investment contract but not to exceed 5 years after initial operation of fixed assets under the work programme.

Table 4.2. **Investment Incentives** *(cont.)*

State in-kind grants **Article 288 of Entrepreneurial Code**	• State in-kind grants may include: land, buildings, structures, machinery and equipment, computers, measuring and control devices and equipment, vehicles (excluding cars), industrial and household equipment. • State land grants are provided for the temporary free use, or granted on the basis of temporary free use with subsequent free transfer to ownership or land use subject to fulfilment of the investment obligations under the investment contract. • The maximum size of the public in-kind grant cannot exceed 30% of the volume of investment in fixed assets of the legal entity.
Investment tax benefits **Article 290 of Entrepreneurial Code**	Tax preferences are available to legal entities of the Republic of Kazakhstan, implementing investment projects, including priority investment projects and strategic investment projects. The types of tax preferences are: 1) investment priority projects: • The decrease of calculated corporate income tax by 100 %; • The application of the coefficient 0 to land tax; • Tax calculation on property at the rate of 0 % to the tax base. 2) investment projects: • Exemption from value added tax on imported components, spare parts, and raw materials under investment projects 3) investment strategic projects: • The decrease of calculated corporate income tax by 100 % from activities under the investment strategic project.
Investment rebate **Article 291 of Entrepreneurial Code**	• Investment subsidy is provided through the compensation of up to 30% of actual expenses on construction works and purchase of equipment, excluding value added tax and excise duties on the basis of supporting documents, but not exceeding the cost of prescribed pre-project documentation with the state expertise in the order established by the legislation of the Republic of Kazakhstan. • Investment subsidy is provided in accordance with the decision of the Government of the Republic of Kazakhstan to the investor implementing priority investment project. • Payment of investment subsidies is subject to the fulfilment of investment obligations by the investor.
Non-tax benefits	Stability is guaranteed in the following circumstances: • Legislation on employment of foreign labour force in accordance with the Code of the Republic of Kazakhstan "On taxes and other obligatory payments to the budget" (Tax code); • The application of "One window" concept.
Conditions for granting investment preferences Article 286 of Entrepreneurial Code	Investment project implemented by a newly created legal entity on certain priority activities, the list of which is approved by the Government of the Republic of Kazakhstan, and providing implementation of investments in the amount of not less than 2 million monthly accounting index established by the law on Republican budget and valid on the date of application for investment preferences. • State registration of a legal entity made no earlier than 24 calendar months before the date of application for investment preferences; • The recipient is the newly created legal entity of the Republic of Kazakhstan, which carries out investments in the amount of not less than 2 million monthly accounting index established by the law on Republican budget and valid on the date of application for investment preferences

Table 4.2. **Investment Incentives** *(cont.)*

List of priority activities	Decree of the President of the Republic of Kazakhstan No. 874, dated 1 August 2014 establishing priority sectors for priority investment projects. Six priority areas, divided into 14 priority sectors are defined: Priority sectors: 1. Metallurgy: - Steel industry - Non-ferrous metallurgy 2. Chemical industry: - Agricultural chemistry - Chemicals for industry 3. Petrochemical industries: - Oil refining - Oil and gas chemistry 4. Mechanical engineering: - Automobile industry - Electrical equipment - Production of agricultural machinery - The production of railway equipment - Mining equipment - Oil and gas production equipment 5. Production of construction materials: - production of construction materials 6. Food industry: - Food production
Incentives in Special Economic Zones (SEZ)	
Qualification criteria	To qualify, a legal entity must: ● Be registered by the tax authorities in the territories of SEZs. ● Have no structural subdivisions beyond the boundaries of the territories of the SEZs ● At least 90% of aggregate annual income must constitute income earned from activities in the SEZ consistent with the objectives of the SEZ's formation. For a legal entity in the 'Park of Innovative Technologies' – at least 70% of the aggregate annual income must constitute income earned from activities in the 'Park of Innovative Technologies'.
Tax incentives	● Exemption from corporate income tax ● Exemption from land tax ● Exemption from property tax ● 0% VAT on goods fully consumed during realisation of activities corresponding to purposes of creation of the SEZ and included in the list of goods established by the government ● Exemption from land use fee for the period specified in the contract of temporary paid land-use (lease), but not exceeding the term of the special economic zone,
Special tax regime for agricultural sector	
	Corporate income tax, value-added tax, social tax, property tax, and vehicle tax payable is reduced by 70% for producers of agricultural products.

Source: Government of Kazakhstan, December 2016.

In December 2016 available incentives included:

- General/common tax incentives, available to all investors, including:
  - Exemptions from customs duties on imported equipment and parts

- State in-kind grants
- Investment allowances for industrial facilities and their subsequent reconstruction and upgrade.

- Targeted incentives for **priority investment projects** into activities established by Decree No. 874 of the President,[2] including:
  - Tax incentives
  - Tax holidays for 10 years
  - Exemptions from land tax for 10 years
  - Exemptions from property tax for 8 years
  - Investment subsidies of 30% of actual expense for installation and construction works, and equipment acquisition
- Special tax regime for **agricultural sector**: income taxes, value added tax, social tax, property tax, and vehicle tax are reduced by 70% for producers of agricultural products.

The government is well aware of the importance of non-fiscal measures in the overall investment-attractiveness of the country and the ultimate success of the diversification efforts. Several non-fiscal measures have been adopted, including visa-free entrance for citizens of 19 countries in 2016, exemption from quota and work permit requirements for foreign individuals in entities holding an investment contract for the implementation of priority investment projects, exemption from local market tests for employers to hire foreign employees to work in SEZs. Additional measures, as discussed in Chapter 5, include state support to different types of firms and activities which may, for instance, involve financial and in-kind support.

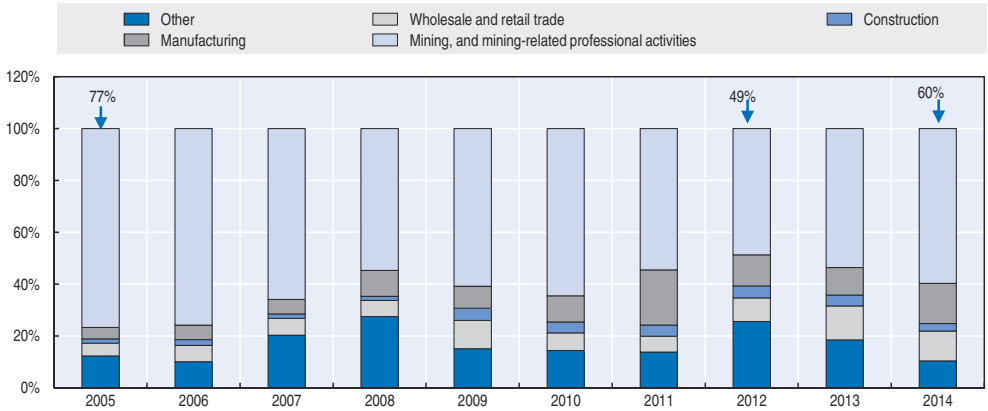
- Non-tax incentives
  - exemption from quota and work permit requirements for foreign individuals of entities holding an investment contract, as well as some of their contractors and subcontractors
  - a stability regime to apply in the event of changes in tax legislation
  - application of the "single window" principle, under which one competent authority – the Investment Committee of the Ministry for Investments and Development – provides the bulk of services, limiting the investor contact other state authorities and reducing the number of documents to be submitted.

Investment incentives are also available to businesses locating in Special Economic Zones (SEZs), in which they enjoy exemptions from corporate income tax, land and property tax, and zero-rated VAT on goods fully consumed during realization of SEZ activities. The first law creating SEZs was adopted in January 1996 to accelerate the country's economic development and its integration into

the world economy by attracting investment and encouraging export-oriented production. Since then the legal framework has changed several times, responding to the changing priorities of the government. The SEZs are now primarily governed by the Law "On Special Economic Zones in the Republic of Kazakhstan" No. 469-IV of 21 July 2011. In 2016, Kazakhstan had 10 SEZs. The existing SEZs can be broadly subdivided into three categories: industrial and manufacturing (e.g. "Astana-New city", "National Industrial Petrochemical Park" in Atyrau region; "Ontustik" in Sairam district of South-Kazakhstan region; development of the chemical and petrochemical industries in the Pavlodar region); service (e.g. "Burabay" in Akmola region), and technical innovation (e.g. "Informational Technical Park" in Almaty).

The investor's response to such a generous set of tax incentives is yet to be evaluated. FDI inflow data, as reported by the National Bank of Kazakhstan (see Figure 4.1), shows the share of FDI flows into mining and mining-related activities at 60% in 2014. The figure bodes well if contrasted against a decade-old composition of FDI flows. The concentration of FDI into the subsoil production was heavier in 2005, with 77% of total FDI going into mining and mining-related operation. However, when the comparison is made with 2012 performance, the picture is less reassuring; FDI inflows in 2012 were more balanced, with more than half of FDI flowing into the non-mining industries. Against the backdrop of considerable volatility in the commodity price cycle through this period and in the absence of any comprehensive evaluation of the effectiveness of Kazakhstan's tax incentives it is difficult to draw any firm conclusions on the relationship between these tax incentives and recent levels of FDI investment in Kazakhstan.

Figure 4.1. **Gross FDI inflows, percent of total**



Source: National Bank of Kazakhstan, *www.nationalbank.kz/?docid=469&switch=english*, accessed December 2015.

StatLink http://dx.doi.org/10.1787/888933452835

Evaluation of the costs and benefits of tax investment incentives

Tax incentives can create inefficiencies and generate distortions in the allocation of resources between different types of taxpayers, different sectors or industries and different types of businesses in favour of those receiving preferred tax treatment. A large and complex array of incentives can add to the complexity of the tax system and can make it harder to comply with and administer the tax system. In addition, in the area of specific investment projects, exemptions may be provided in a non-transparent and discriminatory manner. Another concern over the use of tax investment incentives is the resulting forgone revenue. In 2012, the OECD recommended that Kazakhstan ensure that investment incentives, including in Special Economic Zones, are cost effective. The OECD called for a review by Kazakhstan of the existing investment schemes in light of the OECD *Instrument on Incentives and Disincentives* as part of the *Declaration on International Investment and Multinational Enterprises*, which recommends making investment incentives as transparent as possible so that their scale and purpose can be easily determined.

In 2013, in response to the OECD's recommendation, the Ministry of Finance conducted an assessment of tax expenditures – revenue foregone – attributable to preferential tax treatment of taxpayers. The analysis showed that, based on the 2011 data, tax expenditures amounted to about 2% of GDP. In Kazakhstan, little analysis has nevertheless been conducted to understand the direct and indirect costs associated with the tax incentives. Nor has the effectiveness or cost-efficiency of existing tax incentive programmes in meeting their intended objectives – stimulating investment and driving it towards priority sectors – been properly assessed. Only limited data have been collected on the direct and social benefits to the economy generated by incentives-enticed investment. In the absence of any such analysis, it is difficult to conclude whether these tax incentives have been effective and efficient in attracting additional investment and any associated positive spillovers through technology and knowledge transfer. Cost benefit analysis is a key component of effective incentive administration. Box 4.1 presents core elements of costs and benefits of tax incentives that need to be analysed.

Fiscal incentives granted in the framework of SEZs are a case in point. Despite the effective business facilitation and support measures that can be found in the SEZs in Kazakhstan as assessed in the next chapter of the present *Review*, tax incentives remain a key element of the strategy to attract investors. International experience has shown that while successful zones provide quality infrastructure and a good environment for doing business, they do not always require highly generous fiscal incentives. According to a survey of zone investors in ten countries in 2009, levels of corporate taxation ranked fifth among their concerns, behind cost/quality of utilities, access to transport

Box 4.1. **Conducting an analysis of costs and benefits of tax investment incentives**

When conducting cost-benefit analysis of tax incentives the following components of costs and benefits need to be included in the analysis.

Costs of a tax incentive programme include:

Primary revenue forgone due to tax incentives. The revenue losses associated with the tax incentives could represent a large revenue drain; this foregone revenue needs to be calculated and reported regularly. Estimates of revenues forgone due to tax incentives provide policy makers with the required inputs to inform policy decisions.

Tax planning opportunities. Tax incentives and preferential tax treatments give rise to unintended and unforeseen tax-planning opportunities. The effective tax rate differentials formed by tax incentives open up opportunities to shift taxable profits and deductions across entities with different tax treatments either domestically or internationally, resulting in significant revenue leakages.

Redundancy. The rationale behind tax incentives – to encourage new and additional investment – means that incentives need to be targeted effectively to avoid redundancy. If tax incentives are provided to taxpayers in relation to investments that would have otherwise occurred in the absence of the incentives, then the tax preference provided will provide the investing taxpayer with a windfall gain. Effective tax design can limit redundancy by better targeting incentives to new and additional investment, however, this can also lead to greater complexity and the associated increase in compliance and administrative costs for taxpayers and tax administrations.

Taxpayer compliance costs. Tax incentives impose significant compliance costs on taxpayers in understanding and complying with the tax rules and regulations. Time and money spent by businesses to qualify for and receive tax incentives, as well as to lobby the government for incentives, represent significant indirect costs.

Economic efficiency costs. Providing incentives for certain types of investments is likely to have efficiency costs and distort resource allocation. There is a risk that there will be inefficiently high investment in incentivised activities and inefficiently low investment in others. Incentivised firms are likely to enjoy an artificial competitive advantage, which may also lead to distortions in other markets such as the labour market, where incentivised firms are likely to be able to attract workers from non-incentivised firms by offering higher wages. These distortions are likely to lead to a less efficient allocation of resources.

Administrative costs. The indirect costs of tax incentives, including the administrative costs of running them, could be quite substantial; technical personnel need to be hired or (re)trained to ensure compliance with the rules,

Box 4.1. **Conducting an analysis of costs and benefits of tax investment incentives** *(cont.)*

additional data and information management systems need to be introduced or adjusted. There is also an additional cost of staff and materials required to administer requests for information and auditing of tax accounts to determine if investors are compliant with tax incentives definitions.

Benefits of a tax incentives programme include:

Direct impact and revenue. By reducing the tax burden, tax incentives increase the after-tax return of an investment. That, arguably, encourages additional investment, which may translate into more jobs, higher returns to capital owners and potentially more investment. Greater investment and economic growth results in additional direct tax revenue.

Indirect and induced impact. Through employment and linkages effects, the incentivised investment also generates other income opportunities and corresponding indirect revenue gains. Indirect effects arise from inter-industry transactions, while induced effects are due to changes in income, from spending on local goods and services.

Positive spillover effects, international integration. FDI attracted to the country could generate positive externalities – "spillovers" – for the host economy. Investment can act as a trigger for technology and know-how transfers, but also bring in the "entire package", i.e. needed management experience, entrepreneurial abilities, marketing and sales experience, which can be transferred to the host country by training programmes and learning-by-doing.

Social/environmental benefits. It is often argued that tax incentives can correct for market imperfections. Where the social rate of return on the investment is higher than the private rate of return (e.g. investments into R&D, green technologies or renewable energy), tax incentives could be justified as an instrument to improve the return on the private investment and correct the instances of market imperfections. The benefits of the incentivised investment to the larger society need to be counted in.

infrastructure, regulatory environment for business and trade facilitation (Farole, 2011). For example, Charitar and Narrainen (2009) point to the success of the Shenzhen High-Tech Industrial Park, which attracted some 2 000 firms while offering only very limited fiscal benefits.

The lower oil prices combined with the slower growth in China and the economic contraction in Russia have affected Kazakhstan's export revenues, mounting fiscal pressures and weakening macro-economic fundamentals of the country. Elimination of some tax incentives, designed and introduced at the times of upward-sloping oil prices, could provide a relief to fiscal pressures.

However the revenue generation priority of the government needs to be considered alongside its investment attraction strategy, in a "whole-of-government" manner, to ensure consistency between the country's tax policy and its broader national and sub-national development objectives. Only a thorough analysis of tax-related policies can reveal the effectiveness of the policy measures that the government is implementing to stimulate investment. It is therefore important for the Ministry of Finance to build its human and institutional capacity to conduct cost-benefit analyses, performance diagnostics of tax policies, and tax policy simulation analyses, in order to support informed government decision-making.

Effective tax rates

With non-uniform treatment of business profits, the Kazakh tax policy-makers need to fully understand the likely effect of the diversity of tax regimes on the capital investment decisions of the investors.

When considering capital investment options, investors can be expected to analyse the entire tax landscape of the country. Their first point of reference is the statutory tax rates that serve as an important signal function. The assessment does not end there though. Analysis of the country's effective tax rates allows capturing into a single measure the complex tax landscape of Kazakhstan, including the statutory tax rate, the impact of tax holidays, depreciation allowances and other tax incentives. Effective tax rates further combine investment-related factors, such as the expected rate of business profitability, or the type of assets invested in. The measures express the tax liability as a share of the present value of all financial profits expected from a capital investment. Effective tax rate analysis sheds light on the implications of tax parameters – including targeted tax incentives – on investment returns and helps understanding the implications of implemented (or proposed) tax policy measures on expected investment outcomes.

Two forward-looking effective tax rate indicators are commonly used. The average effective tax rate (AETR) measures the difference in the before- and after-tax net present value of a profitable real investment project. The AETR is relevant in a context where a firm needs to decide among a set of mutually exclusive projects. This is the typical decision faced by a multinational choosing to locate investment in one of the OECD countries. In other words, the AETR affects inbound FDI. The marginal effective tax rate (METR) is the tax component of the user cost of capital and identifies the percentage rise in the cost of capital for an investment project due to taxation. Conditional on locating in that particular country, it affects the scale of investment: a higher cost of capital is associated with lower investment. Like the AETR, the METR depends on both the statutory tax rate and the definition of the tax base, however, the

tax base will generally play a relatively more significant role in the determination of the METR and this largely accounts for the difference in the two measures.

To analyse the divergence of tax burden on capital in Kazakhstan, analysis of effective tax rates of various business segments were conducted. Six representative tax regimes were analysed, as follows:

- **Regime 1:** A project is granted a tax holiday for 10 years; a standard corporate tax rate of 20% is applied thereafter. This regime applies to investment into special economic zones and/or one of the 14 priority sectors.
- **Regime 2:** A project is granted a reduced tax rate of 6% for the life of the project. This regime is applicable to producers of agricultural products, aquacultural (fishery) products, and for rural consumer co-operatives who enjoy a 70% reduction of the standard corporate tax rate.
- **Regime 3:** A standard corporate tax rate of 20% for the life of the project.
- **Regime 4:** A standard corporate tax rate of 20% for the life of the project, as well as full deduction for the capital asset, taken at once within one tax period.
- **Regime 5:** A standard corporate tax rate of 20%. In addition, a branch profit tax, reduced to 5% *under a tax treaty*, applicable to after-tax profit of a foreign company with a permanent establishment in Kazakhstan, resulting in a tax rate of 24%.
- **Regime 6:** A standard corporate tax rate of 20%. In addition, a branch profit tax of 15%, applicable to after-tax profit of a foreign company with a permanent establishment in Kazakhstan, resulting in a tax rate of 32%.

Annex 4.A1 discusses in details the modelling process, as well as underlying data. The table below only presents the results. Table 4.3 shows AETR and METR calculated for investment under each of the six tax regimes

Table 4.3. **Effective tax rates on hypothetical capital investment projects Investment financed by Retained Earnings Profit rate – 20%**

In per cent

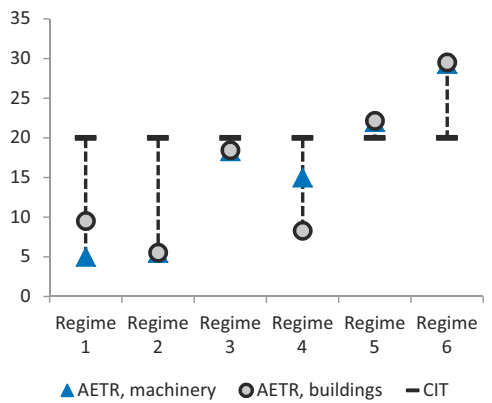
Corporate income tax regime	Machinery and Equipment		Buildings	
	AETR	METR	AETR	METR
Regime 1	5.02	9.46	9.53	11.33
Regime 2	5.50	4.08	5.53	4.22
Regime 3	18.33	14.28	18.45	14.71
Regime 4	15.00	0.00	15.00	0.00
Regime 5	22.00	17.39	22.14	17.89
Regime 6	29.33	23.88	29.52	24.51

Source: Author's calculations.

discussed above to allow for cross-comparison. Two classes of assets are considered: 1) machinery and equipment or 2) industrial buildings. The assumptions, discussed in detail in Annex 4.A1, are used uniformly across all scenarios to ensure that the differences in effective tax rates are attributable only to the changes in tax variables.

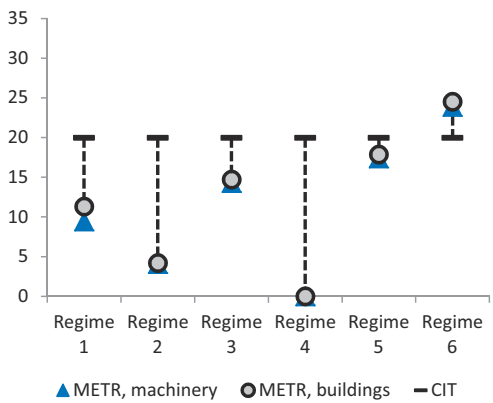
A quick glance at the effective tax rates calculated under various tax scenarios (Table 4.3 above) reveals considerable variation of the tax burden on capital investment across the segments of business investors in Kazakhstan. The results are easier to observe when shown against the statutory tax rate, as seen in Figures 4.2 and 4.3, where the size of dotted lines represents the difference between the statutory and effective tax rates for each tax regime under consideration. The difference between the highest and lowest AETR is as high as 24.31 percentage points for the investment in machinery and equipment financed by retained earnings. The same difference in METRs is 23.88 percentage points. These differences are substantial.

Figure 4.2. **Average effective tax rates (AETR) against the statutory corporate tax rate. In percent**



StatLink http://dx.doi.org/10.1787/888933452848

Figure 4.3. **Marginal effective tax rates (METR) against the statutory corporate tax rate. In percent**



StatLink http://dx.doi.org/10.1787/888933452851

Notes: Investment financed by retained earnings. Assumptions: profit rate – 20%; inflation – 3.5%; real rate of interest – 10%, true economic depreciation – 12.25% for machinery and 3.25% for buildings. Personal taxes are excluded.
Source: OECD.

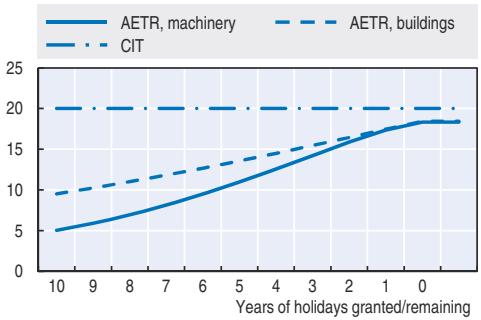
While the effect of significantly lower effective tax rates on targeted investment in Kazakhstan is yet to be studied, the differences in effective rates between various tax regimes open up opportunities to shift activities across entities with different tax treatments either domestically or internationally. This adds further pressure on tax revenues, representing a substantial point of concern for Kazakhstan's authorities.

To show the effect of tax holidays on effective tax rates, the evolution of effective tax rates over the course of tax holidays is studied. Figure 4.4 shows the development of effective tax rates for investment into machinery and buildings, financed by retained earnings. The effect of tax holidays is easily observable; a large one-off investment will benefit the most from the tax holiday regime. However, an additional or repeated investment that could be necessary, for example, for capital replacement, will benefit less as tax holidays become exhausted and the effective rates increase over time. The analysis confirms a well-known argument – tax holidays are most attractive for footloose industries. Short-term investments are likely to benefit from tax holidays compared to longer-term investments. Since tax holidays benefit the industries that start making profits during the holiday period a favourable tax bias exists for short-term projects and short-term assets.

Figure 4.5 offers an interesting insight into the importance of macroeconomic fundamentals. Marginal and average effective tax rates are studied under different inflation rate assumptions. Effective rates under inflation rates of 3.5 (solid lines) are 8.5 (dotted lines) are analysed. A higher inflation rate, more realistic in Kazakhstan's setting, clearly offers a discouraging investment environment, as both marginal and average tax rates are higher under the inflation rate of 8.5. This highlights, once again, the critical importance of macroeconomic factors in business attractiveness of the country.

Figure 4.4. **Development of average effective tax rates over the course of a tax holiday Investment into machinery and buildings, financed by retained earnings**

In per cent

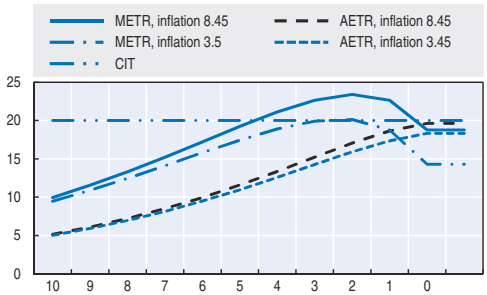


Source: Author's calculations.

StatLink http://dx.doi.org/10.1787/888933452868

Figure 4.5. **Development of marginal and average effective rates effective tax rates over the course of a tax holiday, under different inflation rate assumptions**

In per cent



Source: Author's calculations.

StatLink http://dx.doi.org/10.1787/888933452871

Making the tax system more efficient

For the purpose of enhancing the efficiency of the country's tax system, the government decided at the end of 2015 to scale back or remove some exemptions as part of its plan aimed at consolidating the Tax Code and the Customs Code into one single code. With the same view of making the system more efficient, it also planned to simplify the multi-layered tax regime. Accordingly, a number of amendments are expected to be introduced to the tax part of the new Code, which would become effective in late 2017. In addition to the abolition of tax incentives seen as ineffective or contradicting WTO rules, notably the following tax changes have been announced:[3]

- The current tax regime would be replaced by a three-layer tax regime as follows: A general tax regime; a special tax regime for individual entrepreneurs based on a patent; and a special tax regime for small and medium-sized enterprises and agricultural enterprises;
- Progressive individual income tax rates would be introduced;
- Measures aimed at simplifying and improving the subsurface-use taxation, the real estate taxation for individuals and the social tax procedure.

In addition, the plan includes amendments to optimize tax and customs duties collection, including improving the tax monitoring of large taxpayers and introducing a common procedure for the enforced collection of unpaid taxes and customs duties.

Policy recommendations

Kazakhstan's ambition of joining the top 30 most developed countries by 2050 will largely depend on its ability to create an investment-stimulating business environment, putting in place the ingredients necessary for the private sector expansion, including, more importantly than ever, diversification of investment into non-extractive industries.

Kazakhstan's tax regime is one of the key policy instruments that can either encourage or discourage investment. Like all countries, Kazakhstan faces a trade-off: reducing the tax burden to encourage investment deprives the country of much-needed revenue, in Kazakhstan's case, putting further pressure on its already weakened fiscal position. Despite the growing recognition by Kazakh authorities of the challenges associated with tax incentives, there is inadequate analysis of their costs and benefits in a national context to support the government's decision making. Limited data is collected either on the direct and indirect benefits to the economy, or on the cost of these tax incentives, including forgone revenue. With non-uniform treatment of investors and targeted tax relief no assessment is made in favour of and against such treatment, to ensure that the different treatment can be properly justified.

Businesses complain about costly compliance, inconsistent application of rulings in practice, the lack of predictability, and excessive discretion in tax-related decision-making.

- *Broaden the tax base*. Reversing the recent decline in the government receipts is a priority. This can be achieved by streamlining the tax system and eliminating wasteful tax incentives identified through a credible cost-benefit analysis.
- *Introduce more systematic tax expenditure analysis and reporting*. Regular and consistent tax expenditure analysis is an essential element of good governance. The revenue forgone through tax incentives should be reported regularly, ideally as part of an annual tax expenditure report covering all main tax incentives.
- *Collect better tax revenue data*, as a follow-up to, and in the framework of the OECD Revenue Statistics Project.[4] The analysis of tax incentives required for public statements, budgeting, periodic reviews, tracking of behavioural responses by business, etc. is data intensive. Revenue authorities need to periodically collect and analyse taxpayer data. This may require them to introduce institutional mechanisms to do so.
- *Strengthen policy analysis capacity*. To support coherent and comprehensive government decision-making, the Ministry of Finance needs the capacity to analyse and explain tax reforms' impacts to decision makers and the public. Both, the human and institutional capacity need to be strengthened.
- *Eliminate ambiguity in interpretation of legal provisions*. Statutory guidance needs to be made available to allow for an unambiguous interpretation of domestic and international tax laws. The inconsistency in application of tax provisions, including between various tax authorities and regions, has to be addressed. This will not only improve predictability and clarity of the business framework but also support stable and consistent tax compliance in the country.
- Strengthen tax administration, including the administration of VAT, to enhance tax compliance and to increase the effectiveness and the efficiency of the combat against tax fraud and non-compliance. The government should notably implement administrative reform to tackle VAT refund-related fraud, which appears to be significant, as part of the implementation of broader tax compliance strategy based on risk management principles. Such reform should aim at minimising the revenue losses from fraud and non-compliance without creating undue costs and complexity for compliant businesses.

Notes

1. Effective 1 January 2009.
2. The Tax Code of 2008 abolished the stability of the tax regime for subsurface use contracts other than production sharing agreements (PSA) signed with the government prior to January 2009, contracts which passed the obligatory tax inspection, and contracts signed by the President. All other subsurface users, including those with contracts concluded before 2009, but not stabilized with respect to taxation, are subject to taxation in accordance with the tax law that is in effect at the time when a particular tax liability arises.
3. See Table 4.2. for the list of approved "priority activities".
4. "Kazakhstan: Ministry of Justice approves plans to consolidate Tax Code and Customs Code", *EY Tax Insights*, 5 May 2016.
5. In the framework of the OECD Revenue Statistics in Asia Project, a report by Kazakhstan on revenue statistics is expected to be finalized in the second half of 2016.

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ANNEX 4.A1

The analysis of effective tax rates is using the Devereux and Griffith model (Devereux and Griffith, 2003), extended by Klemm to permanent establishments (Klemm, 2008). The theoretical discussion of the model, as well as its practical application for policy analysis, have been widely documented,[1] and are not repeated here. The discussion below presents only the formulas used in the analysis (without showing the derivation of the formulas) to allow for replication of the results by an interested reader. Economic and tax law data used in the analysis as well as all assumptions made in the course of modelling are presented below.

The calculations are made under the following basic assumptions:

- The hypothetical capital investment is made by profit-making value-maximizing business;
- The business acts in an open economy that takes the world rate of return as given;
- Personal taxes do not affect investment decisions (i.e. analysis is done on the company-level and not on a shareholder-level).

Economic parameters are summarized in Table 4.A1.1 below.

Table 4.A1.1. **Economic parameters assumed in the analysis**

Economic variables	Symbol	Value
True economic depreciation	δ	
Machinery and equipment		12.25%
Industrial Buildings		3.25%
Inflation	π	3.5%
Real interest rate	r	5%
Pre-tax profit rate	p	20%

Essential elements of the Kazakh tax system used in the analysis are presented in Table 4.A1.2 below. Corporate tax rates are shown for *a single corporate tax regime*, applicable, for example, to investment into special economic zones and/or one of the priority sectors. The formulas presented in this Annex are the ones used in modelling of this tax regime.

Table 4.A1.2. **Domestic tax variables used in the analysis**

Tax variables	Symbol	Rate/Notes
Depreciation allowance	θ	Declining-balance depreciation for both, capital investment into machinery and equipment, and buildings.
Machinery and equipment		25%
Industrial Buildings		10%
Corporate tax rate. A single corporate tax regime is detailed below, as an example. Under this regime, the corporate tax rate changes twice over the life of the project.		
Tax holiday for 10 years	rate τ1 for Y1	0%
20% for the rest of the project	rate τ2	20%

It is assumed that the investment is financed by **retained earnings.**

In the model, the AETR is calculated as present discounted value of taxes over the present discounted value of the profit of a project in the absence of taxation. Adopted by Klemm (Klemm, 2008) to permanent investment, rather than one-period perturbation, AETR is defined as:

$$AETR = \frac{R^* - R}{p/(r+\delta)}$$

where R^* is discounted value of the economic rent earned in the absence of taxation, R is the same in the presence of taxation, p is the pre-tax profit (net of depreciation), r is the real interest rate, and δ is true economic depreciation.

R^* – the economic rent in the absence of taxation – is determined as:

$$R^* = \frac{p-r}{r+\delta}$$

As discussed in Table 4.A1.2 above, we consider an investment project with 2 changes in corporate tax rate over the life of the project. In this case, R is determined as:

$$R = \gamma\left(\frac{(p+\delta)(1+\pi)}{\rho-\pi+\delta(1+\pi)}\left(1-\tau 1-(\tau 2-\tau 1)\left(\frac{(1-\delta)(1+\pi)}{1+\rho}\right)^{Y1}\right)-1+A\right)+F$$

where:

$\gamma = (1-m^d)/(1-z)$ is a factor that measures the difference in treatment of new equity and distributions; m^d is a personal tax on dividends and z the tax on capital gains. Since our analysis is conducted on the company-level and not on a shareholder-level, γ is equal to 1.

$\rho = \left(1 - m^{i}\right) i / (1 - z)$ is the investor's discount rate; m^{i} is the personal tax rate on interest and i the nominal interest rate, determined as $i = (1 + \pi)(1 + r)$. In the absence of personal taxes $\rho = i$.

π is the inflation rate

$\tau 1$ and $\tau 2$ are the corporate tax rates applicable to the investment project under consideration, over the life of the project

Y1 is the duration of validity of corporate tax rate $\tau 1$

A is the present discounted value of depreciation allowances. The calculation of A depends on the depreciation rules (see, for example, Abbas and Klemm (2012), or Botman, Klemm, and Baqir (2008) for relevant formulas). We are only reproducing the formula for depreciation allowances under declining balance method applicable to the investment project under discussion.

$$A = \theta \frac{1+\rho}{\rho+\theta}\left(\tau 1 + (\tau 2 - \tau 1)\left(\frac{1-\theta}{1+\rho}\right)^{Y1}\right)$$

F captures the effect of the investment being financed by alternative sources of finance: retained earnings, new equity or debt. Our analysis was limited to the investment financed by retained earnings; $F = 0$ when the investment is financed by retained earnings.

To calculate METR, R is set to zero and solved for a pre-tax net profit $\tilde{p}$ (see, for example, Abbas and Klemm (2012), or Botman, Klemm, and Baqir (2008)).

$$\tilde{p} = \left(1 - A - \frac{F}{\gamma}\right)\left(\rho - \pi + \delta(1+\pi)\right) / (1+\pi)\left(1 - \tau 1 - (\tau 2 - \tau 1)\left(\frac{(1-\delta)(1+\pi)}{1+\rho}\right)^{Y1}\right) - \delta$$

Marginal effective tax rate is calculated as:

$$METR = \frac{\tilde{p} - r}{\tilde{p}}$$

Notes

1. See, for example, Abbas and Klemm (2012), or Botman, Klemm, and Baqir (2008).

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Chapter 5

Investment promotion and facilitation in Kazakhstan

The legal regime faced by foreign investors, the protection granted to them, and the design of the country's tax policy are only a part of the overall investment environment. The quality of domestic regulations and administrative procedures, the incidence of corruption as well as policy transparency and coherence also influence countries' ability to attract and retain investment. Kazakhstan has recently undertaken many steps to improve the quality of its overall investment climate, including through administrative simplification, changes to the regulatory process and efforts to reduce corruption and other forms of unfair treatment of businesses. In many areas it is too early to assess the impact of recent legal changes while, in others, challenges related to implementation and enforcement persist.

Investment and jobs are central to Kazakhstan's economic development agenda and critical in achieving its inclusive growth objectives. Investment facilitation and promotion can, in turn, be powerful means to attract investment and maximise its contribution to job creation, diversification of the national economy, and to provide opportunities for broad-based entrepreneurship. Successful investment facilitation policies reduce the costs of establishing and expanding business operations in the country, for foreign and domestic investors alike, while effective investment promotion helps reduce information asymmetries and attract investors, who might otherwise not establish their operations in the country. Jointly, investment promotion and facilitation policies can help increase the amount, as well as the type of incoming investment, in the host economy. If inadequately designed or implemented, however, they can prove costly for the governments and taxpayers as well as affect the level playing field among the different economic actors, leading to a reduction in the overall welfare.

The previous *Investment Policy Review of Kazakhstan* (OECD, 2012a) made several recommendations regarding the country's investment promotion and facilitation policies (see Box 5.1). For example, concerns were raised about the administrative procedures for business and the quality, predictability and transparency of domestic regulations, in particular in certain areas related to local content policies, hiring of foreign staff, and tax administration, among others. More generally, it was stressed that the quality and predictability of investment-related decisions and creating new regulations could be improved in Kazakhstan. In relation to investment promotion, it was recommended that Kazakhstan evaluates the impact of its existing investment incentive schemes, including those in Special Economic Zones, in order to improve their efficiency. In addition, it was suggested that the government consider whether the fragmented approach to granting investment incentives, administered through the conclusion of individual investment contracts with investors, supports the objectives of transparency embodied in the OECD *Checklist for Foreign Direct Investment Incentive Policies*. Finally, the government was encouraged to improve the institutional framework for investment promotion. All these and other relevant aspects are discussed in this section.

Box 5.1. **OECD 2012 Recommendation on investment promotion and investment facilitation policies in Kazakhstan**

The OECD made, in 2012, several recommendations relating to the country's investment promotion and facilitation policies (OECD, 2012a; 19-20). They relate to four areas, described below in more detail: a) a reduction of administrative barriers for businesses, including in the area of local content and hiring expatriate staff; b) improvements in the quality, transparency and coherence of domestic regulations and predictability of investment policy decision-making; c) better evaluation and administration of fiscal incentives for investment; b) and reconsidering institutional framework for investment promotion to ensure its efficiency, including through possible streamlining.

- Reducing administrative burdens on firms, including in the area of local content and hiring expatriate staff: The *Investment Policy Review* of Kazakhstan recognised the overall progress that the Government made in simplifying administrative procedures for business. It also noted that available business surveys show that one in ten investors mention strict regulations, licenses and approvals as one of top three obstacles to doing business in Kazakhstan (Ernst and Young, 2010). In addition, the *Review* noted three areas where the applicable regulations appeared to be overly burdensome for firms and may be holding investment back –namely local content requirements and the procedures for hiring expatriate staff.
- Improving the quality of domestic regulations and transparency and predictability of investment policy decision-making: More generally, the *Review* noted the need to improve the regulatory transparency, predictability and coherence in Kazakhstan, especially as the country progressively narrows down the coverage of stability clauses in its investment contracts. It was highlighted that the government can improve policy consistency by improvements in the process of drafting new regulations, including by avoiding conflicts and overlaps between existing and new regulations as well as systematising the process of public consultation and *ex ante* assessment of draft regulations.
- Institutional set-up for investment promotion: In regards to investment promotion, the *Review* noted that Kazakhstan's institutional system for promoting, attracting and assisting foreign investment is quite complex as several governmental agencies have related various responsibilities, which are not always clearly delineated. For example, it was not clear how the coordination between the Ministry of National Economy, Ministry of Industry and New Technologies (MID, currently the Ministry for Investments and Development), the national body for investment promotion – KaznexInvest, the Intergovernmental Commissions (IGCs) in charge of trade and economic co-operation, and Investor Service Centres are to co-operate

Box 5.1. **OECD 2012 Recommendation on investment promotion and investment facilitation policies in Kazakhstan** *(cont.)*

and complement each other, rather than compete and dilute the overall effort, both *de iure* and *de facto*.

- Fiscal incentives for investment: Finally, the *Review* stressed the need for improving the transparency, effectiveness and efficiency in the management of fiscal incentives for investment in Kazakhstan. At the time of the previous *Review*, the choice and scope of incentives provided for investment projects was specified on a case-by-case basis through agreements signed by individual investors with the Investment Committee at MID. Such tailor-made arrangements, especially if not systematically published, often lack transparency and run the risk of administrative discretion, with the possibility of differentiated treatment for individual investors depending on their economic weight and local political connections. In addition, systematic evaluation and coordination of the various incentive and state support programmes was lacking, and low administrative capacity and coordination have further reduced their effectiveness.

Investment facilitation

Improvements in the overall business climate and administrative simplification

As already noted in the previous *Investment Policy Review of Kazakhstan* (OECD, 2012a), Kazakhstan has made perceptible progress in pursuing administrative simplification and reducing certain elements of red tape. Indeed, this has featured high on the government's agenda, with several prominent strategies and policies being launched to reduce the administrative burdens on firms (see Box 5.2). These actions have been reflected in the country's improved ranking on the World Bank's *Doing Business* (DB) indicators – from 51st in 2016 to 35th out of 190 evaluated economies in 2017, positioning it ahead of many of other economies in the region (Figure 5.1). Recent improvements were most important in the area relating to dealing with construction permits, getting electricity and starting a business (Figure 5.2). In turn, progress in facilitating trade or getting access to credit has been muted and is explored in more detail later in this chapter (see trade policy and financial sector development).

Most recently, the Law of RK No. 269-V "On Amendments to Certain Legislative Acts of the Republic of Kazakhstan on Issues of Fundamental Improvement of the Conditions for Entrepreneurial Activity in the Republic of Kazakhstan" of 29 December 2014, which came into effect on 1 January 2015, introduced amendments to 119 laws in the country – including the Tax Code, the Civil Code, the Labour Code, the Land Code. It has clarified and simplified

Box 5.2. **Recent administrative simplification efforts in Kazakhstan**

In recent years, the Government of Kazakhstan has launched several initiatives aiming at improving the quality of domestic regulations and reducing the administrative burden faced by businesses (OECD, 2012a; OECD, 2015c). These efforts have predominantly focused on administrative simplification and streamlining of the domestic licences and permits system as well as administrative procedures more broadly, as covered by the Doing Business indicators.

For example, the "Concept of Further Reforming of the Licensing System of the Republic of Kazakhstan for 2012-15" was introduced to simplify procedures to obtain licences and improve the licensing system more generally. The Law No. 269-V "On Amendments to Certain Legislative Acts of the Republic of Kazakhstan on Issues of Fundamental Improvement of the Conditions for Entrepreneurial Activity in the Republic of Kazakhstan" of 29 December 2014 introduced several changes both regarding the process of obtaining licenses and applicable requirements. For example, time periods as well as the number of procedures and lists of documents required for obtaining the permits for construction, business registration and liquidation, bankruptcy have been reduced. Currently, licences are issued in electronic format through the public database "E-licensing" and the time period for issuing licences has been reduced from 30 to 15 days.

In addition, on 20 May 2015, President Nazarbayev announced a set of 100 administrative steps to be undertaken by the government to improve the efficiency of the state apparatus and reduce the administrative burdens placed on citizens and firms to support the country's economic development. The announced measures fall into five broad categories i) creation of a modem and professional civil service; ii) ensuring the rule of law; iii) Industrialization and economic growth; iv) a unified nation for the future; v) transparency and accountability of the state), with over a dozen relating to investment policy. For example, the plan includes strengthening of the post of the business ombudsman to protect the rights of entrepreneurs; integration of customs and tax systems (currently under way); a reform of the tariff system in the regulated services sectors to help attract investors; a reform of the antimonopoly committee to align it with the OECD standards; and several trade facilitation measures, including the implementation of a single window for trade. The full list of measures is available on the website of the President's Administration (*www.akorda.kz*).

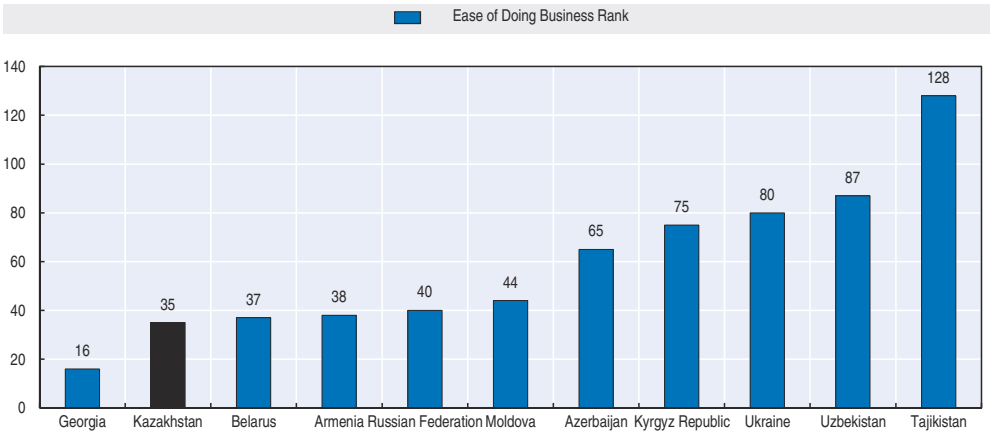
If fully implemented, the measures could significantly alter Kazakhstan's investment climate. The government's implementation capacity is, however, contingent on the ability of the responsible agencies to develop medium to short term action plans, allocation of sufficient human and financial resources,

Box 5.2. **Recent administrative simplification efforts in Kazakhstan** *(cont.)*

including training for the responsible staff, and effective progress monitoring and evaluation. Obtaining feedback from businesses and other stakeholders should be integral in the process to ensure that the reforms' objectives are achieved in practice. Businesses consulted in the process of this *Review* stressed that, in the past, implementation has fell short of official assurances and that high variation of administrative practices and rent-seeking behaviour of implementing officials remained a *de facto* barrier to doing business in Kazakhstan.

Source: The Government of Kazakhstan and stakeholders consulted during the process of the present Review (April 2016).

Figure 5.1. **Overall ease of doing business rank in Kazakhstan and other regional economies, 2017**



Source: World Bank's *Doing Business indicators*, 2017.

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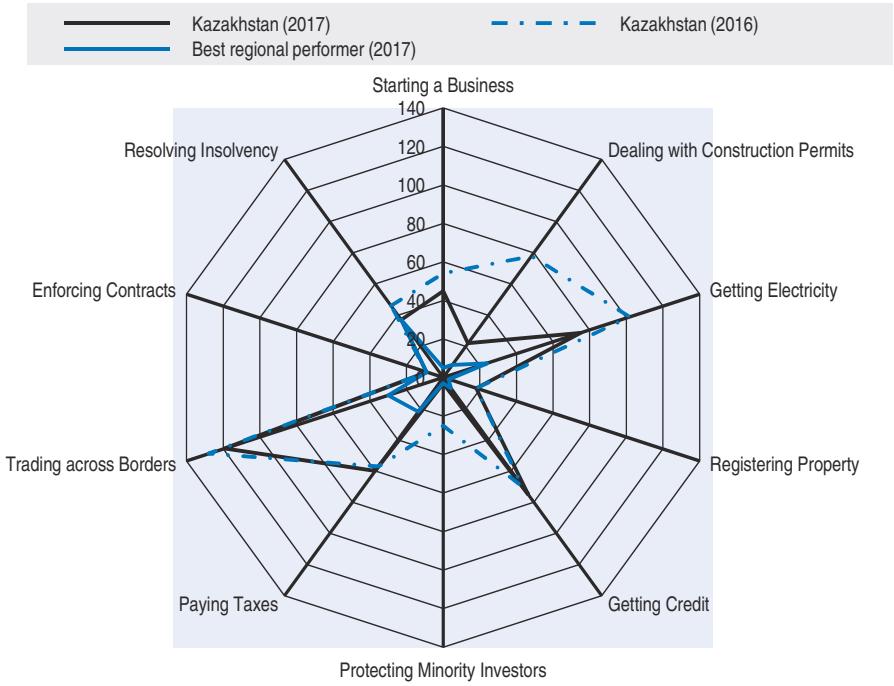
some procedures for obtaining administrative permits and licences, including for small- and medium-sized enterprises (SMEs). The areas targeted by Law No. 269-V, notably those relating to starting or liquidating a business, have contributed to significant improvements in the DB rankings, mentioned above. Also, through that process a number of licences and permits were streamlined or cancelled. According to the Ministry of National Economy, this number reached 153 or 30% of all licences and permits. Currently, 26 activities (and 87 sub-activities) are subject to licensing requirements (Table 5.1).[5] In addition, as highlighted earlier in this *Review* and explained further in Box 5.2, President Nazarbayev announced a list of 100 administrative steps, some of

Figure 5.2. **Kazakhstan's performance on different aspects of *Doing Business* relative to the regional best performer and regional average, 2016-17**



Source: World Bank's *Doing Business indicators*, 2016-2017.

StatLink http://dx.doi.org/10.1787/888933452890

which include measures that can help reduce the bureaucratic burdens placed on firms and improve the efficiency of the state apparatus.

It remains to be seen whether these initiatives will be effectively implemented and whether they translate into better experience by firms as well as improved perception of the business climate in Kazakhstan. In 2013, it took firms 11-30% longer to obtain an operating or import licence in Kazakhstan than it did in other countries in the region (Table 5.2). Once all planned reforms are implemented and new procedures fully operational – including the single window for investors, discussed next, the government could engage in an evaluation exercise, potentially in a form of a firm survey, to verify whether the reforms have achieved the desired effect.

As mentioned above, one element of particular relevance to investment facilitation included been the establishment of a single window for investors in Kazakhstan. Since then, a one-stop-shop (OSS), incorporating some OSS elements, has been established and is administered by the Investment Committee at the Ministry of Developments and Investment (see Box 5.3).[1] It

Table 5.1. **List of economic activities subject to licensing requirements in Kazakhstan, 2016**

List of activities subject to licensing requirements (Law No. 202-V)
1. broadcasting;
2. culture;
3. education;
4. architecture, town building and construction;
5. oil and gas;
6. industry;
7. informatisation and communication;
8. turnover of narcotic preparations, psychotropic substances, precursors;
9. healthcare;
10. use of atomic power;
11. ensuring of information safety;
12. special technical facilities for performance of immediate search measures;
13. turnover of weapons, military equipment and certain types of arms, explosives and related articles
14. turnover of toxic substances;
15. manufacture of the state symbols of the Republic of Kazakhstan;
16. manufacture and turnover of ethyl alcohol and alcohol products, manufacture of tobacco articles;
17. commodities exchange;
18. export and import of goods;
19. financial sphere and activities related to concentration of financial resources;
20. use of cosmic space;
21. gambling business;
22. veterinary;
23. agriculture;
24. transport;
25. forensic expert;
26. services provided for physical persons and legal entities

Source: Government of Kazakhstan (April 2016).

Table 5.2. **Number of days to obtain various licenses in Kazakhstan as compared to other countries, 2013**

	Days to obtain an operating licence	Days to obtain a construction-related permit	Days to clear direct exports through customs	Days to obtain an import licence	Days to clear imports from customs	Days to obtain an electrical connection*
All Countries	30.2	71.1	7.9	18.6	11.8	30.9
Eastern Europe and Central Asia	23.2	72.6	4.8	13.5	5.9	26.6
Kazakhstan	42.9	61.4	7.2	21	11.8	31.6

Source: World Bank's Enterprise Survey database, 2013.

was launched in pilot form in 2015, applying to priority investment projects only, and extended to all firms in 2016. According to the government, currently, the OSS includes 20 physical facilities throughout Kazakhstan, with the main

Box 5.3. **One Stop Shop (OSS) for investors in Kazakhstan and relevant international experience**

The Entrepreneurial Code (EC) of the Republic of Kazakhstan No. 375-V of 29 October 2015 established the principle of a "single window" for investors to be administered by the agency responsible for investment, (i.e. currently, the Investment Committee at the Ministry for Investments and Development). The pronounced goal is to provide "a centralized form of assistance to investors by the authorized body for investment in the provision of public services; minimise investors' involvement in the collection and preparation of documents; and limiting their direct contact with public authorities" (Article 282 of the EC). Currently, the one-stop shop for investors in Kazakhstan is a physical facility, called an Investor Services Centre (ISC), one of which is located at the Ministry for Investments and Development (Address: Kabanbay Batyr Avenue 32/, 1 Transport Tower Building.) In order to access the centre, an investor needs to pre-notify the centre about its arrival and have an identification document during the visit. Altogether, there are 19 ISC offices in 16 cities in Kazakhstan. The information on regional ISCs can be obtained on the Kaznex invest website (*http://invest.gov.kz*). In addition to the Center, there appear to be 19 offices in 16 different cities in Kazakhstan, administered by the State-Owned Corporation "Government for Citizens".

The "single window" approach was launched in 2015 in a pilot form, applying to priority strategic investment projects only, and extended to all firms in 2016. ISC has been developed with the help of PricewaterhouseCoopers. According to the government, investors can obtain through the ISC information on investment opportunities in Kazakhstan; receive assistance in the preparation and presentation of the documents required by different agencies; as well as benefit from support in obtaining the required administrative permits and licences. Currently, the most common services obtained by investors via OSS are: requests of investment incentives, investors visa (C1) requests, business registrations, access to land as well as receipt of permits for geological exploration, construction or hiring foreign staff. The government allows investors to obtain over 300 public services via the ISC and in the near future plans to complement it with an online investor support system that will allow investors to register, receive information and submit applications for permits digitally (*www.baseinvest.kz*).

During the consultations with stakeholders undertaken in the course of this *Review*, it was established that the ISC is still relatively unknown by the businesses operating in Kazakhstan and embassies of top investing countries in the country. It appears that further work could be undertaken in order to familiarise the business community with the services provided by the ISC as well as to obtain feedback as to the features that could be extended or improved.

In addition, as the government is progressing in expanding and operationalising the single window for investors, it could learn from international as well as its own experience in establishing one-stop shop (OSS) solutions in other fields, notably those undertaken by the Ministry of Justice (Janenova, 2009), to avoid common pitfalls and adopt best-practices. Introducing successful OSS solutions is notoriously difficult and involves many challenges related to effective co-operation among agencies, introducing necessary amendments to the legislation, and establishing information-sharing systems and appropriate digital solutions,

Box 5.3. **One Stop Shop (OSS) for investors in Kazakhstan and relevant international experience** *(cont.)*

among others (Sader, 2006; World Bank, 2009; OECD, 2015a). For example, according to the government, currently 13 different ministries as well as authorities at the regional and city level co-operate within the OSS. Joint orders were signed between the participating ministries and regional *akimats*, establishing posts responsible for interaction between ministries and internal follow-up within each agency, together with posts for a delivery of a given public services that involves coordination among the agency. It remains to be seen if this mechanism will suffice to ensure effective coordination in practice, at the central and regional level, as more investors learn about and use the OSS services. Given that effective governmental coordination is a critical component of success of any effective OSS, and also remains the most difficult to achieve, the government should closely monitor the ability of the OSS to deliver permits involving several agencies and the associated delays.

More generally, as the government further operationalises and expands its single window, it should consider what institutional set-up and functional arrangement best suits its needs, and which functions should the OSS perform. The table below provides an overview of different functions that an OSS can have in different countries. Feedback from potential and established investors can play an important role in fine-tuning the design and functions of the OSS, while external advice and capacity building may be helpful to ensure that the choices reflect international best-practices.

Comparative performance of the types of one-stop shops in place in 2010

	No. of countries	Average		
		No. of procedures	No. of days	Ranking (out of 183)
A. Commercial Registry with other bodies on the same site	7	7	24	99
B. Commercial Registry which liaises with other bodies	20	6.7	19	61
C. One-Stop Shop (not a Commercial Registry) which liaises with other bodies	13	6.3	27	98
D. Integrated registration function	12	5.8	13	49
E. Online registration facility	15	5.2	14	48
All countries with one-stop shops	**67**	**6.1**	**19**	**67**
F. Other countries	116	9.3	46	106

Source: Government of Kazakhstan, OECD (2015a),World Bank (2009), Sader (2006).

office located at the Ministry for Investments and Development (Investor Services Centre, ISC) and 19 offices operated by the State-Owned Corporation "Government for Citizens" in different regions. In principle, investors can obtain necessary information, start administrative procedures and obtain permits in these facilities. In the future, there are plans to provide these facilitates online on a dedicated government website (*www.baseinvest.kz*).

As the government increases awareness about the functioning the Single Window among the business community and expands its functions, it could consider reaching out to international organisations, its development partners, and other experts for assistance in implementation as well as to involve local business associations for feedback and promoting the use among the business community. The international experience with the establishment of single windows has shown that the process of setting them up and operationalising them is far from easy, and requires a high level of co-operation among the participating agencies, regular feedback from the private sector as well as a high level of political support to ensure that it becomes an effective "one-stop shop" rather than "one more shop" (Sader, 2006; World Bank, 2009; OECD, 2015; Box 5.3).

In addition, as mentioned at the outset, specific aspects related to administrative procedures were highlighted as particularly burdensome to firms at the time of the earlier *Review* (OECD, 2012a). This related in particular to local content policies but also to tax and environmental regulations. Overall, while important progress has been made in some of these areas, e.g. in the area of local content policies and hiring of foreign staff, with some changes resulting from the country's WTO entry but also broader reforms, several problems remain. For example, businesses report that, despite *de jure* changes to the process of hiring of foreign workers, administrative procedures for obtaining working permits for foreign staff remain complex (see Chapter 2). In the area of tax administration, it appears that tax authorities still lack appropriate capacity and training, which results in varying interpretation and application of law as well as rent-seeking opportunities. Even in the case of administration of fiscal incentives, the goal of which is to encourage and attract investment, large delays in distribution and retroactive changes in administrative decisions are said to complicate rather than facilitate investment decisions of firms. All in all, while Kazakhstan has made important progress in improving several elements of the administrative procedures, as reflected in its improved business rankings, several specific issues still remain problematic to foreign and domestic investors alike.

Quality of regulations

Changes to the country's investment climate captured by World Bank's *Doing Business*, explained above, do not necessarily reflect the quality, transparency, and predictability of investment-related policies, nor the consistency in their implementation. Therefore, reforms that focus primarily on improving such rankings may miss the mark in terms of improving the aspects of investment climate that have highest incidence on firm investment decisions. For example, the empirical cross-country studies examining the impact of improving *Doing Business* indicators on increasing FDI inflows have found mixed results.[2] Meanwhile, the impact of strong institutions, high regulatory quality and control of corruption on FDI is found to be significant in numerous studies.[3]

In 2012, the OECD *Review* highlighted that the predictability, coherence, and quality of regulations and administrative procedures remain problematic in Kazakhstan (OECD, 2012a: 20, 63-66). Business stressed that input on draft regulations was not sought systematically, and: "there are cases when only a fraction of stakeholders are invited to participate in public discussion, or draft law or regulation is provided to stakeholders for input and comments just before it is sent to parliament". Hence, at that time, two most important challenges related to the need for more systematic stakeholder consultations and the conduct of *ex ante* impact assessment of draft laws and regulations.[4] Since then, Kazakhstan implemented several reforms in these and other areas related to regulatory policy, highlighted briefly below, and described in more detail in the *OECD Regulatory Review of Kazakhstan* (OECD, 2014) and *OECD Integrity Scan of Kazakhstan* (OECD, 2017, forthcoming).

For example, several laws were passed to better regulate the right of the public to be informed about and comment on draft laws and regulations.[5] The new Entrepreneurial Code and the Law No. 480-V "On Legal Acts" of 6 April 2016 also regulate the participation of business entities in rulemaking in Kazakhstan, including the possibility of accredited business associations to submit suggestions on draft laws on regulations through the Expert Council for Private Enterprise.[6] Advances in the provision of e-government services have also allowed the government to make draft laws and regulations available to the public and obtain inputs from citizens via a dedicated website (*www.egov.kz*).[7] Currently, consultations take place most commonly via public councils and online consultations with the wider public.

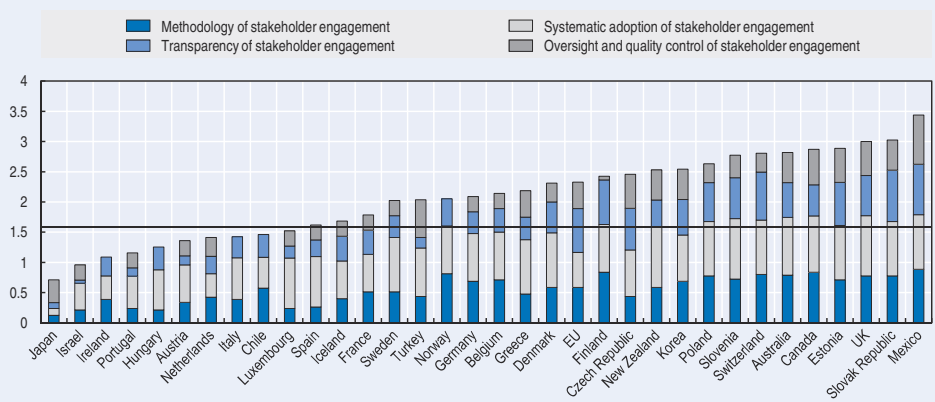
While this process involves certain elements of a consultation mechanisms found in OECD countries (Box 5.4), it still distant from the concept of pro-active and open stakeholder consultation. For example, selection criteria for participation in public councils remain unclear, potentially increasing the risk of policy capture, and commenting periods are limited (OECD, 2017, forthcoming).[8] The government could also take a more pro-active stance towards public consultations, using an explicit call for comments and providing more guidance to public officials; as well as consider if current procedures for the private sector involvement do not unduly limit involvement of some businesses in the consultations process. While the government of Kazakhstan appears to be increasingly involving various stakeholders, including private-sector representatives, in the process of preparing draft laws and regulations, implementing some of the recommendations identified above could help reduce the risk of public capture and increase the openness of the decision-makings process.

When it comes to the regulatory impact assessment (RIA), the Entrepreneurial Code has made RIA an obligatory element of developing new regulations and legal acts in Kazakhstan.[9] This is in line with an earlier

Box 5.4. **Overview of relevant best practices in stakeholder consultation in the OECD countries**

Based on the 2014 *OECD Survey of Regulatory Indicators*, a majority of OECD countries have adopted systematic stakeholder engagement practices and require that stakeholders are consulted in the process of developing new regulations. Overall, a systematic conduct of public consultations open to general public, engaging general public in both early and later stage of consultation, setting minimum periods for submitting comments, and, finally, having a formal procedure for taking comments received into account and providing feedback to participating stakeholders reflect the best practices and have a positive impact on the scoring presented below.

Stakeholder engagement in the OECD countries, 2014.

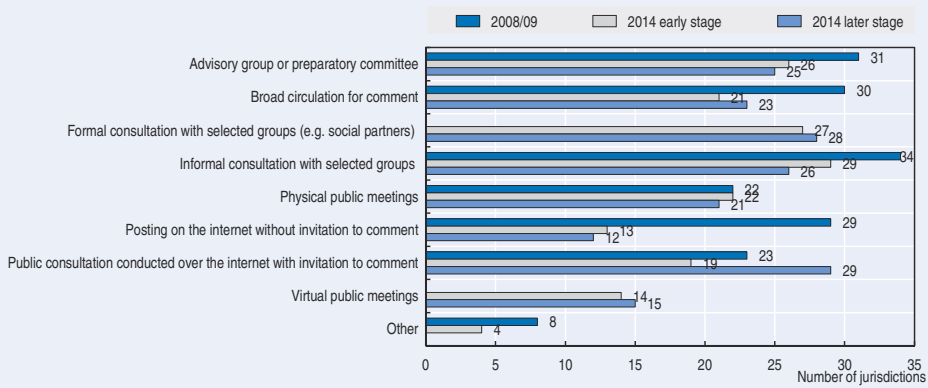


Note: The results apply exclusively to processes for developing primary laws initiated by the executive. The vertical axis represents the total aggregate score across the four categories. The maximum score for each category is 1 and the maximum aggregate score 4.
Source: 2014 Regulatory Indicators Survey results, *www.oecd.org/gov/regulatory-policy/measuring-regulatory-performance.htm*.

The figure above shows the different types of consultation processes and their changing usage. Some tools, e.g. public meetings, are used consistently in all stages of the process. Other tools are used more frequently early (e.g. advisory groups or preparatory committees) or later in the stakeholder engagement process (e.g. posting draft regulations on the Internet or formal consultations with social partners and all interested stakeholders). Limiting consultations to the "usual suspects" through targeted consultations (i.e. over-relying on meetings with special groups), let alone groups accredited by the government, as is the case in Kazakhstan, may discriminate against small and medium-sized enterprises (SMEs), new entrants, and foreign traders and investors (OECD, 2014a; OECD, 2015b).

Box 5.4. **Overview of relevant best practices in stakeholder consultation in the OECD countries** *(cont.)*

Type of consultation



Note: Based on data from 34 countries and the European Commission. Early stage stakeholder engagement refers to a situation where consultations are undertaken to discuss the nature of the problem and to inform discussions on possible solutions. Later stage consultation refers to stakeholder engagement where the preferred solution has been identified and/or a draft regulation already issued.
Source: 2014 Regulatory Indicators Survey results, *www.oecd.org/gov/regulatory-policy/measuring-regulatory-performance.htm*. For more information, consult the OECD website: *www.oecd.org/gov/regulatory-policy/measuring-regulatory-performance.htm*.

recommendation made by the OECD (2014).[10] Still, to reap full benefits of RIA, it should be undertaken using a standard methodology at an early stage of the regulatory process by well-trained public officials and be open to public consultation (i.e. attached to the documentation for public consultations). This will help ensure that RIA is used to inform rather than justify public decisions, and that all costs and benefits of proposed regulations are taken into account. Finally, ensuring that RIAs are of adequate quality in practice will require clear administrative procedures for public officials, allocation of adequate resources and training to responsible staff as well as due supervision and monitoring of RIAs quality. Progress in these areas would bring the country closer to the good practices enshrined in the OECD 2012 *Recommendation on Regulatory Policy and Governance* (OECD, 2012b).

Overall, the government has taken steps to improve the quality of domestic regulations and involve outside stakeholders more in the process of making new legal acts and regulations. Still, the businesses consulted in the process of this *Review* highlighted that poor-quality and inconsistent regulations as well as irregularities in their interpretation and application

remain problematic and continue complicating investment decisions by firms.[11] Further improvements to the process of assessing the impact of draft regulations and strengthening process of stakeholder consultations could be considered. This will help ensure that various stakeholders, including smaller domestic enterprises, can offer their inputs on planned legal changes and voice their concerns, reducing the risk of strong *ex post* reactions by specific stakeholders or the larger public, as observed most recently. While foreign investors dispose of additional consultation mechanisms with the government that allow them to discuss their specific concerns, such as through the Foreign Investor Council (FIC, see Box 5.5), small and medium-sized enterprises and other domestic firms do not benefit from such additional points of contact with the government and, hence, may gain most from improvements described

Box 5.5. **Mechanisms for dialogue with foreign investors in Kazakhstan**

The Foreign Investors Council (FIC), created in 1998, is currently the main forum for direct dialogue between the authorities and foreign investors to address critical issues related to the country's investment activities and the business climate (*www.fic.kz*). It is chaired by the President of the Republic of Kazakhstan and includes, on the government side, the Prime Minister, Chairman of the National Bank and several key ministers (Foreign Affairs, Industry and Trade and Budget Planning), as well as the chairman of the Committee on Investment of the Ministry of Industry and New Technologies. The latter also forms the executive body of the FIC.

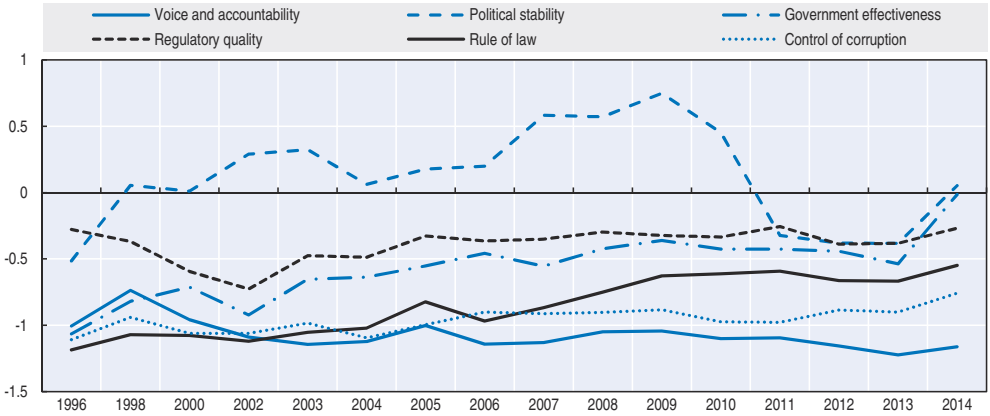
Foreign investors are represented by high-level officers from the banking sector, energy, manufacturing, telecommunications legal and consulting companies and international financial organisations (EBRD, Eurasian Development Bank, Asian Development Bank). To become a member of the FIC, interested foreign companies have to submit their application to the Committee on Investment. The main criterion is the amount of foreign investment in Kazakhstan (USD 100 million for investors operating in the Subsurface sector, USD 25 million in other sectors). Representatives of international organisations involved in Kazakhstan can also participate in the FIC. The FIC has several specialised working groups, including on oil and gas, legal matters, taxation and investment image enhancement. The working groups hold regular meetings and report to the FIC plenary sessions conducted twice a year. The Council has proposed various actions and made recommendations to encourage economic modernisation and local development, to improve the qualifications of local staff and to simplify tax and administration procedures.

In addition to FIC, the government also established a Council for Improving the Investment Climate chaired by the Prime Minister whose goal is also to consult with investors and suggest reforms that can help address investors' concerns and, more generally, lead to improvements in Kazakhstan's business climate.

Source: OECD Investment Policy Review of Kazakhstan (2012) and the Government of Kazakhstan.

above. Finally, improvements in this area, together with wider efforts to combat corruption and improve the rule of law (described at the end of this chapter) can help translate into firms' improved perceptions about the quality of business climate the country (see Figures 5.3-5.4)

Figure 5.3. **Kazakhstan's scores on the Worldwide Governance Indicators (WGI), 1996-2014**



Note: Estimate of governance (ranges from approximately -2.5 (weak) to 2.5 (strong) governance performance).
Source: World Bank World Governance Indicators (WGI) database (2015).

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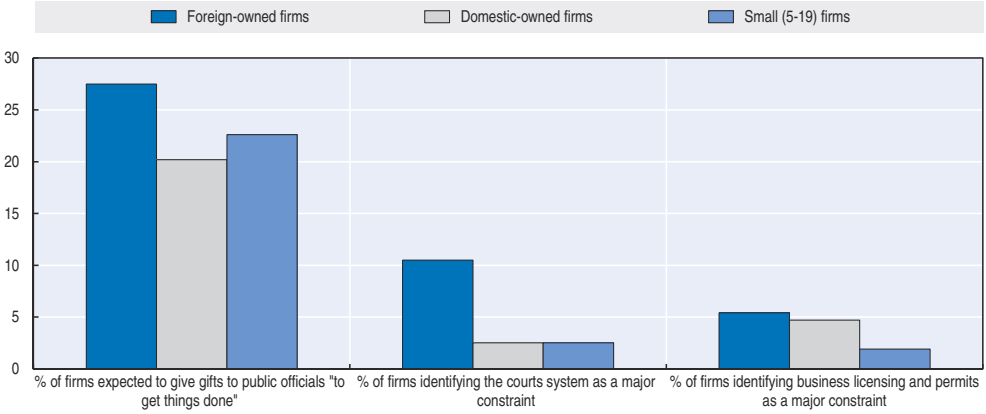
Figure 5.4. **Perception of business obstacles by foreign, domestic and small firms in Kazakhstan, 2013**



Note: Results are based on interviews with business owners and top managers in 600 firms undertaken in 2012-13.
Source: World Bank's Enterprise Survey results, 2013.

StatLink http://dx.doi.org/10.1787/888933452918

Investment promotion

Investment promotion strategy

As described in detail in the previous *Investment Policy Review* (OECD, 2012a), Kazakhstan has a number of programmes in place that aim to support private sector development, investment and entrepreneurship. The broad orientations for the country's development strategy are provided by the President's *Vision 2050*[12] and a ten-year "Strategic development plan till 2020",[13] whose implementation is supported by five-year development programmes called State Programmes on Accelerated Industrial and Innovative Development (SPAIID). The current SPAIID spans the period of 2015-19[14] and identifies a list of sectors considered to be priority sectors.[15] The country's investment promotion strategy inscribes itself into these strategic documents (see Box 5.6).

Box 5.6. **Strategic objectives of Kazakhstan's development and investment promotion policy**

The "Vision 2050" outlined by the President in January 2014 provides the broad vision and objectives of the national development strategy in Kazakhstan (Nazarbayev, 2014). The "main goal [of the strategy] is to join the group of 30 most developed countries: by 2050". Multiple targets are included in the strategy, relating to annual GDP growth and per capita income and other aspects of well-being such as safety, peace or life expectancy (Nazarbayev, 2012). In addition, rates of investment, scientific research, productivity, share of SMEs in the economy and standards of living of OECD countries are considered a "natural benchmark for Kazakhstan" in realising the Vision (Nazarbayev, 2014).

The "Strategic Plan till 2020" outlines in more detail the country's strategic objectives relating to economic development.[19] These include: i) improving business climate, supporting financial sector development, and improving the legal framework; ii) accelerating economic diversification, including through support for priority sectors and creating favourable economic environment; iii) investment in education, healthcare and labour force; iv) improving social protection and quality of housing; v) and ensuring inter-ethnic harmony, political stability and security. Some of the Plan's targets and measurable objectives are relevant to investment policy and include, for example, an increase of domestic and foreign investment in non-extractive sector by at least 30%, an increase of the share of FDI in GDP by ten percentage points; and entry of Kazakhstan into a group of 50 countries with best World Bank's Doing Business indicators by 2020. A monitoring and evaluation mechanism is also put in place with some elements available in English on the government's website. It is, however, unclear what methodology is used either for setting of the quantitative targets or the evaluation of the progress in their implementation.

Box 5.6. **Strategic objectives of Kazakhstan's development and investment promotion policy** *(cont.)*

Five-year programmes, called State Programme on Accelerated Industrial and Innovative Development (SPAIID), support the implementation of the long-term strategic objectives outlined above, the current one spanning the period 2015-19. The overall goal of the programme is to "facilitate the ascension of a private investor in the manufacturing industry" and "create attractive conditions for private investment" (Government of Kazakhstan, 2014). The plan builds on seven broad priority sectors identified in the Vision 2050[20] and sets a more detailed list of specific sectors and associated activities that are considered to be a priority.[21] For each of the sectors, the programme identifies key strengths of the Kazakh industry; key factors impacting competitiveness in these sectors as well as important global players, including potential foreign partners, and sets broad tasks and targets for implementation. It also foreshadows the creation of a specific investment promotion attraction policy. In addition, the plan also includes several investment facilitation measures, such as the establishment of a visa-free regime for investors from OECD countries; creation of the office of business ombudsman and a single window for investors (described in the previous section). Finally, it also highlights the importance of aftercare services provided to investors through a network of Investor Service Centres (ISC).

The country's investment promotion strategy depends and inscribes itself into this framework. The strategy for the previous period has been outlined in the "Programme for Investment Attraction, Special Economic Zone ('SEZ') Development and Export Promotion in the Republic of Kazakhstan for 2010-2014" (OECD, 2012a: 77). It appears that the objectives for the current period are outlined in order No. 406 of the Minister for Investments and Development, which established a sectoral Action Plan for investment attraction for 2016. It is not clear how the plan builds on the results achieved in the previous periods, and whether the change in the time period covered (from four to yearly plans) has been a conscious change in the government planning and monitoring framework.

Source: Government of Kazakhstan.

Until the end of 2014, the main orientations of Kazakhstan's investment promotion were outlined in a four-year investment attraction strategy ("Programme for Investment Attraction, Special Economic Zones' Development and Export Promotion in the Republic of Kazakhstan for 2010-14"). That strategy had built on the SPAIID programme (2010-14), identifying actions to be undertaken in the area of investment promotion to support the development of priority sectors. Since then the approach appears to have changed: instead of a

four-year investment attraction strategy, the Ministry for Investments and Development – responsible for strategic planning in the area of investment policy – adopted a new sectoral investment attraction strategy for 2016.[16] The plan aims to attract investment in support of the country's industrial development plan notably by i) increasing fixed-capital investment in the non-resource sector by 105% relative to the previous year; ii) and attracting new companies listed on the Forbes Global 2000 list. Among others, it proposes to extend the list of priority sectors for which investment preferences are granted as well as proposes actions aiming at investment facilitation (notably through the creation of the OSS and the role of investment advisors in selected embassies abroad and five offices of Kaznex Invest) as well as increased investment promotion and attraction efforts and co-operation with investors.

In addition, as mentioned earlier, the government also approved a "Plan on the Improvement of Investment Climate", including measures to address issues identified as problematic at the time of the previous OECD *Review*.[17] Some of these measures related to investment attraction and facilitation policies. For example, the plan calls for a greater activism of units charged with investment promotion abroad (including actions to be undertaken by Kaznex Invest, investment advisors abroad and Government Council for investment attraction, see later section on the institutional set-up), and refers to a possible provision of exceptional investment preferences.[18] It also lists measures aiming to facilitate investment, notably through facilitated migration and other administrative procedures for foreign staff and improved enforcement of tax and customs legislation. In order to policy coherence and implementation, it would be advisable that the relationship between this roadmap and other existing (or planned) documents aiming to attract and facilitate investment is clarified (such as the Sectoral Plan of MID), including the respective roles of different institutions involved; and that different agencies and ministries are aware of the plan and their respective tasks; and one clearly identified institution monitors progress and ensure effective coordination of different activities. Overall, it appears that Kazakhstan lacks a comprehensive framework for evaluating costs and benefits of different investment promotion and facilitation initiatives and a clear monitoring and coordination mechanism in place. This risks creation of multiple structures that lack efficiency or transparency, compromising the overall goal of investment attraction, pronounced to be the government's priority. Given the centralised character of Kazakhstan's administration, it could be considered whether an agency or taskforce reporting directly to the President's or Prime Minister's Office could not be charged with monitoring of progress and ensuring that agencies co-operate in practice.

The various strategic documents listed above together with the Entrepreneurial Code of 2015 and the implementing decrees establish the general scheme of state support for investment in Kazakhstan. The

Entrepreneurial Code outlines the concept and the types of investment preferences available for investment, and provides the legal definition of investment projects that are eligible for investment support, including priority and strategic investment projects (Article 284 and 286), while government decrees establish the list of priority activities and strategic projects referred to in the Code.[22] The different incentives available for investors in Kazakhstan are described in detail in Chapter 4. Despite the existence of the general framework for investment support, explained above, the choice and scope of certain incentives are still specified on a case-by-case basis in Kazakhstan via agreements signed by individual investors with the Committee on Investment under the responsibility of the Ministry for Investments and Development (MID), as already highlighted in OECD (2012a). The adoption of the new Entrepreneurial Code in 2015 has not changed this *status quo*.[23] The terms and conditions of the contracts as well as the allocated incentives are not publically available, which may limit the transparency of these provisions. In 2015, 44 contracts were signed by investors with MID.[24]

In addition, investors complain that certain incentives for priority investment projects are available only to newly-established legal entities.[25] As a result, new projects or project extensions undertaken by existing investors in the priority sectors are not be eligible for the additional state support dedicated to priority investment projects. Given that in many countries firms tend to engage in more complex or high value-added activities such as R&D after having operated in the host economy for a longer period of time (OECD, 2008), this may pose a barrier to the realisation of the goals enshrined in the country's economic development and investment promotion strategy. In addition, some investors highlighted that the administrative process of allocating incentives remains intransparent and opens scope for corruption possibilities and arbitrary treatment, with some cases of *ex post* recollection of investment incentives causing an uncertainty in project implementation. If that is the case, the irregularities in the administration of fiscal incentives could reduce the attractiveness of the use of incentives in the first place, and dissuade rather than encouraged investment, hence undermining the policy objective. The government could consider if some changes to its investment promotion framework suggested above, including improvements in transparency of the incentives' allocation process and potential reconsideration of the definition of priority investment projects would not serve better its announced policy objectives.

Available instruments of state support

Besides the specific investment preferences, government programmes provide a range of different instruments of state support, such as subsidies for loan interest payments, loan guarantees, industrial infrastructural development,

training of personnel and other in-kind contributions, for which both foreign and domestic-owned investors are eligible, if they fulfil the relevant criteria. These different instruments are outlined in the SPAIID programme (Government of Kazakhstan, 2014) as well as the country's Entrepreneurial Code.[26] In particular, Article 92 of the Code specifies that state support can be provided to different types of firms and business activities, and in particular small- and medium-sized enterprises (SMEs), agribusiness and non-agricultural activities in rural areas; industrial innovation; special economic zones; and investment projects, among others. State support can involve financial and in-kind support (including through the provision of a physical property); institutional support (including through creation or financing of a dedicated financial, research and development or other institution that provides services that are beneficial to firms) and informational support (Article 93).

Overall, the financing of the various investment projects is primarily channelled through the Development Bank of Kazakhstan (for big infrastructure projects, loans are at least KZT 30 million or USD 165 000), Baiterek National Holding and particularly the DAMU Entrepreneurship Development Fund (for financial support of SMEs) as well as KazAgro (for financial support to rural and agricultural areas) (OECD, 2016: 142). There are also several specific programmes designed to support financing and growth of SMEs, described in more detail below.[27] According to the recent OECD *Review* analysing the country's industrial and development programmes, a well-structured overview of all programmes together with their coordinated objectives, status of implementation and evaluation results is missing in Kazakhstan (OECD, 2016: 142). Consequently, the multitude of development programmes currently in place is not sufficiently coordinated nor assessed against their objectives in a systematic fashion, which has compromised their efficiency. For example, about 30% of projects under the SPAIID 2010-2014 have failed (OECD, 2016). If the government wishes to ensure that public resources are not wasted and deliver good value for money, it could consider verifying if the introduction of two recent institutional innovations dedicated to better programme monitoring and coordination has helped reduce the ratio of failed programmes and improved take-up by firms (as well as their subsequent better performance).[28]

Pro-SMEs schemes

In its first *Review* of Kazakhstan's investment policy, the OECD observed that, in spite of the government's declared support of SMEs, existing pro-SMEs schemes did not sufficiently address SME needs and the contribution of SMEs to Kazakhstan's economy remains low. It further noted that access to bank loans by SMEs remained difficult and prohibitive interest rates hampered the expansion of small firms, even if these firms had economically viable projects. The OECD thus, recommended that Kazakhstan "further expand access of

SMEs to financing", in particular through the development of technical expertise in banks "so that banks can properly assess the risks in lending to SMEs and better adapt their services to meet SME needs" (OECD, 2012a).

Since then, the government launched several economic support programmes, each of them focusing on the provision of subsidised loans to SMEs. The first programme for 2014-15 provided for KZT 1 trillion (USD 5.5 billion) to be used primarily to relieve credit problems in the banking and providing subsidised loans to SMEs.[29] In addition, the programme "Nurly Zhol" (Bright Path) for 2015-17 (a stimulus package of USD 14 billion, co-financed by international financial institutions to help the country overcome the difficulties related to the drop in oil revenues) is also meant to be used to continue providing subsidised loans to SMEs. Two other financing programmes have also been reoriented or expanded in reaction to the economic downturn to support SMEs' access to financing (see Box 5.7). In the case of some of these programmes, it is too early to assess their impact on the economy, given that they have been launched or altered relatively recently. The government could nevertheless undertake their mid-term review to assess the level of take-up by SMEs and initial performance results. Overall, comparative analysis of the SME sector in Kazakhstan shows a noticeable lag of contribution of SMEs to the national economy (see Figure 5.1 below and OECD, 2013).[30] While changes to the productive tissue of the economy are long-term processes, and take several years to yield results, the government should monitor and evaluate the effectiveness of the recently introduced SME support programmes and continue advancing on other reforms that aim to facilitate business registration (see investment facilitation section) to assist a healthy growth of the SME sector.

Box 5.7. **Recent programmes implemented in Kazakhstan to facilitate financing by SMEs**

One of the recent tools to support entrepreneurship in Kazakhstan and its regions is a Unified Program for business support and development, i.e. so-called "Business Road Map 2020".[32] The aim of the programme is to support entrepreneurial activity in Kazakhstan, and in particular the development of SMEs, through the provision of loan guarantees, lower interest on loans or in-kind capacity building support. The development and growing capacity and specialisation of SMEs in different regions is meant to support the implementation of the national cluster policy set up in 2013.[33]

In addition, in accordance with the "Anti-crisis action plan to ensure economic and social stability in the years 2016-18", approved by the minutes No. 51 of the Government meeting on December 8, 2015, the state support under the Business Roadmap was reoriented to target any new or on-going investment projects, which provide a 10% increase in permanent jobs, production

Box 5.7. **Recent programmes implemented in Kazakhstan to facilitate financing by SMEs** *(cont.)*

(or services delivery) output and tax payments in comparison to the period prior to project implementation to expand take-up. Moreover, additional funds (KZT 7 billion) are to be allocated to the "Business Road Map 2020" programme, of which KZT 5 billion are to subsidize the interest rate and 2 billion tenge used for loan guarantees.

Finally, as part of the anti-crisis measures for 2016 announced by the government, additional KZT 200 billion are to be allocated towards financing of SMEs working capital and refinancing of loans through the second-tier banks, of which: KZT 100 billion for the priority sectors of the economy (with the ratio of 50% for working capital and 50% for refinancing loans); and KZT 100 billion for the financing of SMEs needs regardless of their nature. The funds will be provided to the Single Pension Savings Fund and the list of financial instruments and second-tier banks to participate in the programme are to be determined in accordance with the Fund's investment policy.

According to the government, action in 2015 focused on implementing an appropriate regulatory framework for the disbursement of state support provided for the Roadmap. In the second stage, in years 2016-19 the government aims to implement an annual monitoring framework. In order to assist in the realisation of these plans, it could be useful for the government to consider publication of the list of beneficiaries of the programme as well as the programme's mid-term evaluation towards the end of 2016.

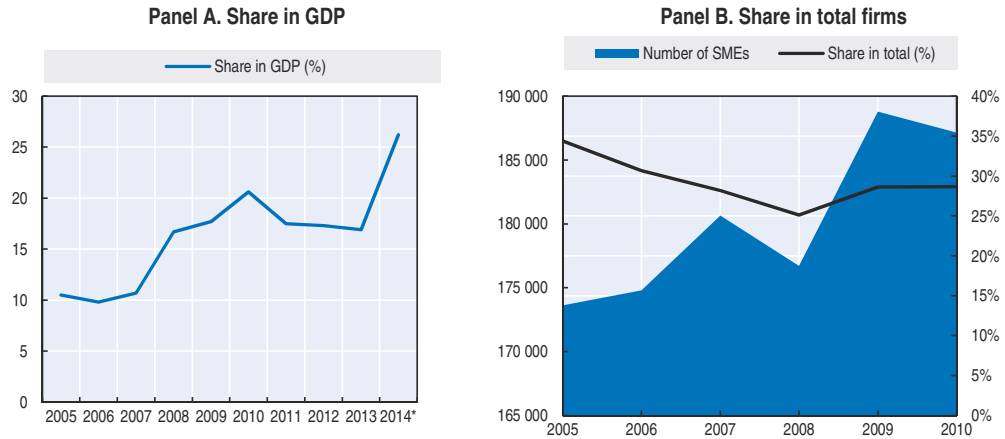
Note: For more information, please see *www.damu.kz* and *www.business.gov.kz*.
Source: Government of Kazakhstan.

Overall, as highlighted in OECD (2016) and elsewhere,[31] a well-structured overview of the various private sector development programmes, including those directed at SMEs, is missing in Kazakhstan, and implementation monitoring and impact assessment mechanisms are not systematically employed. This can undermine the effectiveness of the programmes in place, and reduce the government's ability to improve programmes over time (OECD, 2015). Nevertheless, as will be outlined in the following sections, the government has invested in self-evaluation in several areas related to investment promotion, in particular in relation to the management of SEZs and operations of its investment promotion agency (Kaznex Invest), following which reforms have been undertaken to overcome the lacunae identified in the process.

Special Economic Zones

As seen in Chapter 4, special economic zones (SEZs) are another vehicle through which Kazakhstan aims to attract foreign investors, and facilitate

Figure 5.5. **The importance of small and medium enterprises in the Kazakhstan's economy, 2005-14**



* Data for 2014 as based on a new definition of an SME, introduced as of 1 January 2014, based on the number of employees only (Law dated 10.07.2012 No. 36-V "On amendments to some legislative acts of the Republic of Kazakhstan on the reduction of permits and optimization of control and Supervisory functions of public authorities").

Source: www.stat.gov.kz.

StatLink http://dx.doi.org/10.1787/888933452921

economic development of different regions. Currently, there are ten SEZs in Kazakhstan (see Box 5.8 for more detail).[34] Recognising the fact that the quality of infrastructure (both within the SEZ and its connectivity with the outside transport routes), as well as the quality of the legal and administrative framework for trade and business facilitation within the zones is an important factor influencing the attractiveness of SEZs for investors (see e.g. Farole, 2011), the government undertook a thorough audit of the operations of its SEZs in 2013. Thanks to the audit, undertaken with the help of a private consulting company, several weaknesses of the current SEZ framework have been identified, including weak infrastructure, poor management and a deficient legal framework. The OECD 2012 recommendations have also highlighted that Kazakhstan should seek to ensure cost effectiveness and transparency of its SEZ to ensure they achieve their intended objectives (OECD, 2012a: 19). Consequently, the government has implemented an action plan that resulted in the introduction of amendments of the Law on SEZ as well as other pieces of relevant legislation, including the Tax Code (currently under further reform as seen in Chapter 4).[35]

A primary focus of the recent reform has been the establishment of a single focal point at the level of the central government – currently at Kaznex Invest – to allow for better monitoring of the functioning and performance of SEZs; improved planning of individual managing companies activities and improvement in their management practices and procedures; planning and

Box 5.8. **Special Economic Zones in Kazakhstan**

Special Economic Zone (SEZ) is a part of the territory of the Republic of Kazakhstan with precisely defined boundaries with a special legal regime for implementation of priority activities. The SEZs are now primarily governed by the Law "On Special Economic Zones in the Republic of Kazakhstan" No. 469-IV of 21 July 2011, most recently amended in 2015 to introduce several improvements in the management and operations in the SEZs.

There are currently ten SEZ in Kazakhstan:

1. "Astana - New City" in Astana
2. "Ontustyk" in Sairam District of South-Kazakhstan region
3. "Seaport Aktau" in Aktau
4. "Park of innovative technologies" in Almaty
5. "Burabay" in Akmola region
6. "National Industrial Petrochemical Technology Park" in Atyrau region
7. "Saryarka" in Karaganda region
8. "Khorgos Eastern gate" in Almaty region
9. "Pavlodar" in Pavlovdar
10. "Chemical Park of Taraz" in Dzhambul oblast

Currently, the main infrastructure of three of the above-mentioned SEZs is finished, namely that of SEZ "Saryarka", SEZ "Ontustik" and SEZ "Burabay".

Enterprises operating in the SEZs are exonerated from the corporate income tax, land and property tax, value-added tax fully consumed during realization of SEZ activities as well as customs duties and land use fee. Enterprises registered in SEZs also benefit from several procedural benefits, including facilitated procedures for hiring foreign staff and easier customs clearance procedures (given that goods located and used in a SEZ are exempt from customs duties and taxes, non-tariff measures and any bans or restrictions placed on CU goods). Finally, within the boundaries of the "Park of innovative technologies", firms can benefit from an exemption from social charges provided that labour costs for a given corporate income tax period constitute not less than 50% of the total annual income and that 90% of expenditure on labour costs are salaries of employees that are residents of the Republic of Kazakhstan. The maximum period of application of such benefits is 5 years from the date of registration as an enterprise within the SEZ territory.

In order to be able to operate within an SEZ, an enterprise must be registered by the tax authorities in the territory of SEZ; have no structural subdivisions beyond the boundaries of the territories of SEZ; and at least 90% of aggregate annual income must constitute income earned from activities in the SEZ

Box 5.8. **Special Economic Zones in Kazakhstan** *(cont.)*

consistent with the objectives of the SEZ's formation. For a legal entity in the 'Park of Innovative Technologies' – at least 70% of the aggregate annual income must constitute income earned from activities in the 'Park of Innovative Technologies'. In turn, enterprises that are users of subsurface resources; produce excisable goods (except if engaged in manufacturing or assembling of excise goods under sub-paragraph 6) of Article 279 of the Tax Code); are engaged in form of gambling activity; or, finally, seek the use of other special tax regimes or have used the investment tax preferences in the past cannot register in the SEZ.

Source: Government of Kazakhstan.

development of SEZ infrastructure, identification of fraud; as well as provision of the overall marketing support and assistance in identification of new projects. Meanwhile, individual trust management companies are responsible for the management of individual zones. The government's commitment to reform is welcome as is its use of the private sector's expertise in the design of the reform in this area. Given that Kaznex Invest is still a maturing agency, grappling with several different mandates, and that SEZs' management reforms tend to be challenging due to the existence of possible vested interest groups, it is recommended that the government pays attention to the progress in implementation of the reform, possibly through periodic reporting to the parliament or to the responsible ministry (i.e. MID).

In relation to management of SEZs, Kazakhstan is also tied by certain commitments that it made in the process of its WTO accession. Namely, from the date of Kazakhstan's WTO accession, SEZs and free warehouses in Kazakhstan will need to be established, maintained and administered in conformity with the provisions of the WTO Agreement, including TRIMs (see Chapter 6 on trade policy).[36] This means that, upon expiration of the transition period negotiated by Kazakhstan (1 January 2017), no firms registered in SEZs and operating in free warehouses–new or existing–would be subject to export performance, trade balancing, or local content criteria requirements, in law or in practice.[37] Kazakhstan has also made other broader commitments relating to the pursuit of its industrial policy, including the use of subsidies. For example, Kazakhstan committed to removing or modifying all subsidies programmes, including provisions contained in its development programmes, which fall within the scope of Article 3.1 of the WTO SCM Agreement, so that any subsidy provided would not be contingent, *de jure* or *de facto*, upon export performance, or on the use of domestic over imported goods.[38] This may require some changes to the design of the current and future programmes for the purposes of private sector development in Kazakhstan and has led the government to

introduce certain legal changes in relation to the use of local content policies applied to investment contracts in certain sectors and SEZs. This highlights the need for an innovative approach to promoting linkage creation between foreign and domestic firms, described at the end of this section.

Institutional set-up for investment promotion in Kazakhstan

Another aspect of investment promotion policy that was highlighted as potentially undermining the efficiency of government efforts at the time of the previous *Review* (OECD, 2012a), and where the government undertook reforms, is the institutional set-up for investment promotion. Currently, the Ministry for Investments and Development (MID) is the main government body responsible for the formation of the national investment policy, provision of state support for investors and coordination of implementation of the investment policy in Kazakhstan. This marks a change from a previous review when one ministry was responsible for investment policy design (i.e. Ministry of Economic Development and Trade, MEDT) and another for implementation (i.e. MID) (OECD, 2012: 81). In some areas, the Ministry co-operates with the Ministry of National Economy, previous MEDT, and other relevant ministries, but it is currently the principal ministry in charge on investment policy formation and coordination.

In regards to implementation, Kaznex Invest is the country's national investment and export promotion agency. Its responsibilities include export promotion, in particular in non-oil sectors; search for investors and attraction of FDI into priority sectors; trouble-shooting and support for investors; promotion of Kazakhstan's image abroad; and, as of recently, the management of SEZs. The experience of various OECD and non-OECD countries shows that national and state level investment promotion agencies play an important role in facilitating investment, and helping the government mobilise investment into priority sectors (e.g. Harding and Javorcik, 2007). The degree of success in investment attraction varies, however, significantly depending on the character and effectiveness of the investment promotion agency (IPA) involved (including its function, organisational structure, mandate, financial and human resources at its disposal) as well as the institutional set-up in which it operated and a monitoring and evaluation framework that it is subject to (OECD, 2015a).[39]

Kaznex Invest is a relatively young IPA, having acquired its investment promotion functions in 2010. As such, the agency is still grappling with defining appropriately its core mandate and adjusting its strategy, institutional structure, staffing policy, operations, and modalities of co-operation with other government bodies. Recognising the need to learn from international best-practices and to adapt its internal processes, Kaznex Invest has recently undertaken an audit of its operations by the OECD. The goal of the exercise was to assess the current level of the agency's efficiency in attracting FDI as well as to identify principal factors that may hamper it, through a comparison with

selected benchmark agencies from other countries (see Box 5.9 for more detail). It was established that, compared to the benchmark agencies, Kaznex Invest records currently a low rate of FDI attraction (of 5%) as a result of its actions.

Box 5.9. **Investment Promotion Agency of Kazakhstan – Kaznex Invest: how well is it doing?**

Kaznex Invest was created in 20087 as the export promotion agency of Kazakhstan in an effort to support the goal of economic diversification. In April 2010, its mandate has been altered so that besides the export promotion function the agency became the sole Investment Promotion Agency (IPA). Since then, it performs both of these functions and is the sole coordinator of Special Economic Zones (SEZ) in Kazakhstan. It also hosts a database on investment projects and foreign investors in the country and in co-operation with Investor Support Centers (ISC) supports investment promotion in the regions.

The agency is set up as a joint stock company in which the Investment Committee of the Ministry for Investments and Development (MID) owns 51% of shares and 49% is owned by the National Chamber of Entrepreneurs of the Republic of Kazakhstan "Atameken". It has joined the World Association of Investment Promotion Agencies (WAIPA) in 2011. In an effort to boost Kaznex Invest's effectiveness in attracting investors into the key strategic sectors, the government of Kazakhstan has requested from the OECD an audit of Kaznex Invest operations and a benchmarking vis-à-vis the best practices encountered in other agencies to make the necessary adjustments in its mandate, structure, or operations (OECD, 2015).

One of the strongest findings of the report was the low efficiency of Kaznex Invest vis-à-vis the best performing agencies. For example, only 5% of total FDI inflows were estimated to have been directly generated by Kaznex Invest in 2013 as compared to 11% in Nicaragua or 33% in Czech Republic, for example. The relatively poor performance has been identified in the report to be linked to the relatively large mandate of the institution, which resulted in lesser attention given to investment promotion and facilitation; its focus on serving the needs of the ministry rather than investors; and a lack of clear strategy and well-identified priority sectors and key performance indicators that would be outcome rather than process oriented and in line with the pre-identified strategy.

Source: Government of Kazakhstan and OECD (2015).

One important finding of the OECD audit was that the agency remains primarily oriented towards servicing the needs of the Ministry (i.e. MID) – e.g. through the preparation of reports on FDI trends, tracking changes in various investment climate indicators, such as *Doing Business* ranking, and explaining government investment attraction policies–rather than dealing with investors,

assisting them, and addressing their concerns. As such, it was suggested that the agency reorient its functions to allocate more attention and specialised staff towards generating investment leads and addressing investors' concerns. The development of the new strategy for 2016-19 may be an occasion to address some of these issues, including through an appropriate choice of main objective and Key Performance Indicators (KPIs).

In addition, it will be important that the agency's functions as well as *modus operandi* with other relevant organisations and government agencies is clearly defined. Currently other governmental institutions in Kazakhstan have similar, if not overlapping, functions as Kaznex Invest. For example, several national institutes have functions that are relevant for investment promotion.[40] At the level of the regions, akims (i.e. regional governors) are responsible for assisting in attracting investment into the regions as are Investor Support Councils (ISC) with whom Kaznex Invest supposedly co-operates. In addition, in the past Intergovernmental Commissions (IGCs) were charged with developing relations with target countries (OECD, 2012a: 81-82). It appears that a special Government Council is also charged with the coordination of major investment projects, dialogue with large MNEs, and works towards attraction of MNEs into Kazakhstan through a wide network of offices abroad.[41]

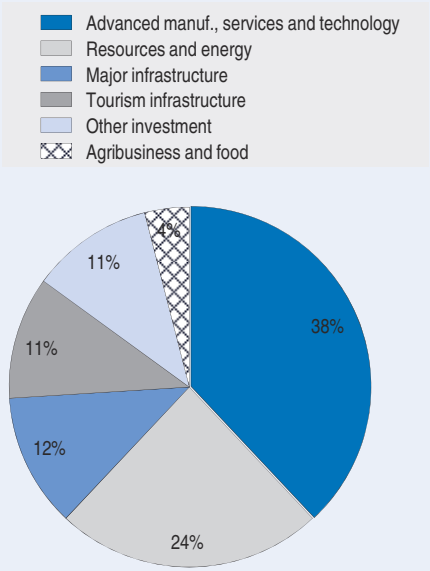
Most recently, following presidential instructions to attract investment, the Ministry for Investments and Development (MID) and the Ministry of Foreign Affairs defined a list of ten priority countries to which the two ministries are to appoint a special advisor[42] while Kaznex Invest is also planning to open offices in five countries.[43] Given that some of these countries overlap and that the government Council appears to dispose of a large network abroad, it would be advisable for the government to consider how complementarities can be achieved and the various institutions can co-operate and interact to increase impact and reduce costs. While advanced IPAs tend to have a well-developed network of foreign offices,[44] many countries assign an investment advisor from the IPA to operate in the premises of an existing bilateral diplomatic unit (e.g. embassy) or other existing government agency to optimise costs, especially at the initial stages of the agency's operations. Overall, in order to achieve results, the government will have to avoid distraction in its investment promotion activities and ensure the actions are well planned, in tune with the overall investment promotion strategy as well as well-coordinated and executed. If given the necessary political support, the MID could play an important role in coordinating various investment promotion activities, providing a clear strategy and roadmap as well as a monitoring framework to assess the actions of implementing agencies. The example of a monitoring and evaluation framework used by the Australian government for its investment promotion activities could provide an inspiration in this regard (Box 5.10).

Box 5.10. **Austrade and National Investment Priorities in Australia**

The Australian Trade and Investment Commission (Austrade) leads a national, whole-of-government strategy for FDI and trade promotion in Australia. The agency's performance in attracting investment into the priority sectors[45] is evaluated under the Australian Government's outcomes and programmes framework. As part of that process, Austrade's Portfolio Budget Statements identify the outcomes and associated deliverables and key performance indicators (KPIs); while the annual reports evaluate the agency's performance against these specific outcomes. The results of that assessment are available, on a yearly basis, online (*www.austrade.gov.au/About/Corporate-Information/AnnualReport*).

According to the Annual Report, 89% of Austrade-assisted investment outcomes were in the five agreed priority industries (see the figure below); while non-priority industries constituted 11 % of outcomes (with the majority being in retail, water management, transport and logistics, and media). Among the KPIs used to measure its performance, Austrade uses number of investment outcomes facilitated (92 in 2014-15, which marks a 28% increase since the previous reporting period); amount of capital expenditure associated with the FDI outcomes facilitated (7.75 billion in 2014-15); the number of new jobs created/retained as a direct result of investment outcomes facilitated (17 685) and the anticipated annual exports from investment outcomes facilitated ($14.5 million). As part of the Annual Reports, detailed information on financial expenditures are also reported and explained, which helps track costs and the agency's efficiency over time.

Austrade-assisted investment outcomes by industry sector, 2013-14



Source: Australian Trade and Investment Commission (*www.austrade.gov.au*).

Box 5.10. **Austrade and National Investment Priorities in Australia** *(cont.)*

In addition to this annual exercise, periodically, the government undertakes a deep review of the agency's actions, using Austrade client, investor and customer data (more than 80 000 firm records), annual client survey's conducted by Austrade and targeted interviews of other government, business and industry stakeholders. As a result of such a review in 2011, the agency has been reformed, changing the agency's structure, operating model and structure. All the information listed above is publically available on the Austrade's website.

Finally, more attention could be given, at the level of the IPA, not only to investment promotion and improving the image of Kazakhstan as an investment location, but also to trouble-shooting, aftercare services, dialogue with investors, and eventually policy advocacy. While Kazakhstan disposes of other fora for discussion with investors to improve the business climate, in many OECD and non-OECD countries IPAs can play a valuable role in sustaining regular working-level contact with investors, gathering their feedback as well as coordinating with other agencies to resolve problems and facilitate investment (OECD, 2015; UNCTAD, 2008; UNCTAD, 2007; Morisset and Andrews-Johnson, 2004). It can also be a useful go-to agency for smaller foreign investors and domestic firms, which encounter hurdles or lack information on available opportunities and state support but do not benefit from access to high levels of the government. It could, therefore, be considered how the functions between the various institutions involved in dialogue with investors could be usefully divided and made complementary, and what role would Kaznex Invest would *de facto* play in that process. In particular, once the single window for investment is implemented and managed by Kaznex Invest, the IPA will start gaining significant information about the usually encountered problems and bureaucratic constraints faced by investors, which could be a potent source of information for its investment facilitation and policy advocacy role. Last but not least, as described in more detail below, the agency could also play a more active role in facilitating contacts between foreign firms and local producers, including through making available the planned database of local suppliers and multinational enterprises operating in various sectors in Kazakhstan (*www.baseinvest.kz*), as well as tailored matchmaking events.

Creation of effective linkage programmes

One important function of a country's investment promotion efforts is the creation of linkages between domestic firms and foreign investors. Such linkages not only help embed investors more in the local economy, allowing for greater investment retention, but also facilitate the development of local skills and capacities, and ultimately contribute to economic growth (OECD, 2015). An

IPA can play an important role in this regard, allowing for creation of business linkages between foreign and domestic firms, for example, through matchmaking events and development of databases of MNEs and local suppliers, co-creation of specific supplier development programmes as well as advocacy for wider reforms, often in collaboration with other government agencies. According to one study, 43% out of 123 IPAs from 109 countries surveyed had linkages programmes in place (UNCTAD, 2006); and a recent survey confirms that linkages creation is perceived as a primary objective by nearly half of responding IPAs (Farinelli, 2015).

Especially as the government appears to move away from reliance on local content requirements (see Chapter 2), it could consider alternative ways in which it can support the creation of business linkages between local domestic and foreign-owned firms. Some of them may involve targeted activities by the IPA (or other agency), while others may require further broader reforms. Examples from several OECD and non-OECD countries can provide some ideas on successful policy approaches that promote local content in a voluntary manner and through strong engagement of investors. For example, since 2001, Australia has been using voluntary Australian Industry Participation Plans (AIP), in order to monitor and encourage local industry's participation in the supply of goods and services to the mining sector (See Box 5.11). The programme has a voluntary character, but according to the government, a high degree of political attention and frequent monitoring, in particular in large projects, has helped ensure that local sourcing amounts on average to 86% of total expenditure in the sector (Government of Western Australia, 2011).

Box 5.11. **Australian Industry Participation Plans**

The Australian Industry Participation (AIP) National Framework – established in 2001 – supports supply chain development in the mining industry by requiring Australia industries to be given "full, fair and reasonable access" to opportunities deriving from significant public and private investment projects (including mining operations).

AIP policy obliges investment projects to compile an AIP plan to set out how they will provide full, fair, and reasonable access to opportunities for Australian suppliers. While not mandatory for operating, an AIP plan – approved by Austrade (Australia's Trade and Investment Promotion Agency) – is a requirement for firms that wish to apply for tariff concessions on eligible imported goods under the Enhanced Project By-law Scheme. AIP plans must show evidence of consultation with Australian manufacturers to determine existing local capacity. Criteria included in the assessment of an AIP plan include, among others: employment creation; skills transfer; regional economic

Box 5.11. **Australian Industry Participation Plans** *(cont.)*

development; technology transfer and R&D; and "full, fair and reasonable opportunities" for suppliers to tenders.

In light of the information about recently declining local content in goods and services in the mining sector, in 2010 the Department of Commerce of Australia commissioned an independent assessment of the ability of the local steel fabrication industry to secure module contracts from energy and mineral projects, followed by a similar study of the local engineering and design industry. Results of firm surveys and market analysis confirmed that changed market conditions and increased competition reduced the share of local content in these and associated industries. For example, in offshore energy projects, local industry participation has fallen from a peak of 72% to an estimated 45%-55% for some projects. As a result of these changes, the Government has decided to revamp its local content programme, both at the national and state level.

For example, in July 2012, reforms to the AIP program were implemented, which included, among others, a requirement for plans and outcomes to be published and a requirement for projects accessing the import duty programs to increase the level of detail provided to Austrade in their AIP plan (e.g. provision of more comprehensive evidence on opportunities being made available to Australian industry.

Australian states also engage in creation of active linkage programmes. For example, the state government of Western Australia through its Industry Capability Network of Western Australia (ICNWA) maintains a local supplier database, matches the inquirer's specified requirements with competitive local manufacturers, provides company profiles and assists in writing specifications and tender processes to facilitate local participation. The service is publically funded and free of charge for participating firms. Due to changes to the way multinational search for (e.g. utilising their owned supplier databases) and contract local firms, the mandate of INCWA has been under review. The state also gives other market intelligence tools at disposal of local firms and has recently engaged in an overhaul of training policy and engaged in policy dialogue with the federal Government regarding facilitated access to skilled labour through temporary and permanent visa programmes.

Source: Farole (2014), Warner (2011), Government of Western Australia (2011).

In this context, the government could consider retaining the monitoring system of local content that it currently has in place, as administered by the National Agency for development of local content (NADloc), even once mandatory requirements are phased out. It can help the government track the evolution of the local content over time as well as serve as an awareness-

raising tool to be used in conversations with investors, as is done in some other resource-rich countries, as Australia. It could also be considered by the government how NADloc and Kaznex Invest can coordinate their activities in the area of promoting the use of local content by foreign investors to benefit from complementarities and avoid undue duplication. For example, the planned development of the database of local suppliers and MNEs operating in different sectors by Kaznex Invest could help local and foreign enterprises learn about the locally available opportunities, and may benefit from the information and expertise already gathered by NADloc and other national institutes.[46] In addition, these activities can be complemented with active matchmaking events, which facilitate in practice the development of business contacts among firms.

In some cases, it is the lack of certain skills, technology, or sufficient quality that hampers the ability of local suppliers to provide goods and services to MNEs present locally. In this case, the IPA, MID or other government agency can engage in facilitating creation of specific capacity-building programmes for local firms, often developed and implemented in close collaboration with investors. The case of Chile provides an example of a private-sector led supplier development programme, led by a large multinational in the mining sector (BHP Billiton), which has been developed in co-operation with the government (Box 5.12). The programme has allowed Chile to increase the ratio of exports to imports in the mining sector from 7 to 50% in only ten years (McKinsey Global Institute, 2013). The co-operation with an MNE not only allows ensuring that the types of skills or capacities that the workers gain are indeed sought after and can lead to creation of employment or business opportunities later on. They can also help reduce the cost of such training programmes if the MNE also contributes some resources, even if in-kind through availability of its specialists and staff.

Box 5.12. **BHP Billiton-led World Class Suppliers' Programme in mining in Chile**

The World Class Suppliers' model encourages mining companies to identify areas where innovative solutions could assist operational efficiency across its operations, and identify local suppliers who have the capacity to work on the problem. Each prioritized challenge is weighted and advertised to suppliers. The selection procedure is rigorous: for example, only 16% of identified projects at CODELCO reached implementation stage. Selection criteria include economic benefit, replicability, urgency of the problem, technological risk, and impact on the operation in the fields of health, safety and environmental standard (HSE). A cluster of 2-3 local suppliers is then created to research the problem and pilot new innovations. In addition to technical funding and support

Box 5.12. **BHP Billiton-led World Class Suppliers' Programme in mining in Chile** *(cont.)*

for the area of innovation, some companies such as BHP also employ external consultants to provide training on organisation and managerial competence and support supplier linkages with local universities.

The project is coordinated by Fundación Chile, a non-profit corporation that aims to support technology transfer and innovation, and increase the competitiveness of Chilean firms across the economy, but does not provide funding for the projects themselves. Fundación Chile has also produced a guide for mining companies undertaking World Class Supplier projects and a detailed handbook is also in development. The guide includes practical advice for companies in the operationalization of the project. As of 2012, 70 cluster projects were under way from BHP and CODELCO and there is interest from the Peruvian and Colombian mining industry. BHP is also currently working on ways to clarify intellectual property rights for innovations developed under the cluster program.

Source: Barnett and Bell 2011; Urzua 2011.

Malaysia also provides a good example of how linkage formation can be facilitated by active skill development- and training programmes, which help bridge the capacity gap of local suppliers and workers, including at a regional level (see Box 5.13). Malaysia implemented several successful national-level linkage programmes aiming to bring together foreign and local firms (e.g. Industrial Linkage Programme[47]). Within that process, it was identified that skills gap of the local population were an important obstacle to effective linkage formation. Consequently, several training and supplier development programmes were put in place. For example, the Global Supplier Programme, guided by 23 MNEs, trained 813 employees from 225 SMEs in its first year alone. It has been implemented in coordination with state-level initiatives, such as the Penang Skills Development Centre (described in Box 5.13) that was a private-public initiative in the region of Penang that aimed to, and successfully helped, reduce the supply-demand skills mismatch in the local industry. This model, which builds on a strong collaboration between the business, government and academia has proved effective in bridging the skills gaps that ensued in a rapidly industrialising economy, and can provide some inspiration to the Kazakh Government. Similar examples can be found in Singapore and Ireland in 1980s and 1990s where the two respective national development agencies played an important role in fostering supplier development programmes, implementing targeted educational programmes in the local educational institutions and advocating for a larger policy reform aiming to improve the level, and adequacy, of qualifications of the local population.[48]

Box 5.13. **The Penang Skills Development Centre (PSDC)**

The Penang Skills Development Centre (PSDC) was established in May 1989 as a not-for-profit training and development centre. At initial start-up, the PSDC received support from the Penang State Government in the form of subsidised rental of premises and an annual training grant for the centre. As it grew in relevance it attracted the attention of the federal government. Starting from 1993, the PSDC received capital grants to assist with its capacity building expenditure such as equipment and machinery. The PSDC invites membership from the manufacturing and related industries and to-date has a member base of 130 companies. With strong support from the government and industry, the PSDC undertook the facilitation of effective resource utilisation amongst the manufacturing and service industries.

The PSDC does not target any specific group and is accessible to all who wish to pursue lifelong learning. Its staple programmes such as those conducted on behalf of the government and the degree and diploma programmes offered under continuous education tend to attract: i) secondary school (high school) leavers; ii) unemployed graduates; and iii) the existing workforce which requires re-skilling and skills upgrading. The success of the PSDC is also attributable to its tripartite business model which draws on the involvement of its three key stakeholders: industry, academia and government. The PSDC is managed and led by the industry and is supported by national academic bodies and the government.

Six government agencies were involved in launching the PSDC: i) the Ministry of Entrepreneur & Co-operative Development (has since then been dissolved); ii) SME Corp; iii) the Standard and Industrial Research Institute of Malaysia; iv) the Penang Regional Development Authority; v) the Penang Development Corporation; and vi) the Penang State Secretariat. These agencies represent the various interests of the government such as local enterprise development, research and development and both state and national level development initiatives. More importantly, their involvement in the PSDC council enables the PSDC to understand the policy directions of the government and therefore, to implement and introduce new human resource development initiatives which complement national policies.

Source: OECD (2011).

Overall, in most cases, successful local content and linkages programmes have involved a close co-operation with the private sector to help forge strategic partnerships with foreign investors to develop local skills and facilitate interactions between these firms and MNEs. They also have been accompanied by continued reforms and adequate funding in the areas of education, innovation, and research and development to facilitate the creation of a

domestic knowledge system (OECD, 2011; World Bank, 2013; McKinsey Global Institute, 2013; Ramdoo, 2015).[49] While the IPA can influence some of these factors, notably through provision of information on the already existing suppliers, facilitating matchmaking as well as targeted training, financial support or other capacity-building programmes; other factors – such as MNE global sourcing strategies or the quality of the overall national education or infrastructure – lie largely outside of its control. Table 5.3 summarises this issue in conceptual terms. In such cases, the agency can still play a powerful role by surveying existing and potential investors regarding the obstacles to engaging with local partners and, whenever applicable, engaging in policy advocacy with the relevant institutions, whenever broader reforms (such as educational reform) are necessary. In order to allow the broader reforms to take place, strong political support at the highest level of the government is required to allow the various ministries long-term reform and co-operation to achieve the desired results. Kazakhstan, with its high political stability and centralised government, would be well positioned to provide such support.

Table 5.3. **Factors influencing formation of MNE-SME linkages – An illustrative list**

Demand for linkages	Supply of linkages	Interaction
	Non-policy factors	
• MNE strategies, parent-affiliate relations, • MNE affiliate characteristics • Type of sector or activity	• Local firms' characteristics • Local market structure	• Trust and social capital • Language and cultural barriers
	Policy factors	
• Ownership requirements • Local content requirements • Tax policies and other incentives • Trade policies • Special Exporting Zones (SPEs)	• Education policies • Financial sector development • Venture capital funds • Other private sector development programmes • Clustering and maturity of local business associations • R&D and innovation policies	• Regulatory environment (e.g. ease of enforcing contracts) • Quality of infrastructure (roads, utilities, ICT, standardisation and certification systems, etc.) • Promotion of local engagement through CSR and RBC • WTO rules relevant to investment promotion
	Role for an IPA	
• Targeting investors prone to engaging with local suppliers or having existing supplier development programmes • Negotiating with incoming investors and offering incentives • Surveying investors on the barriers to engaging with local suppliers • Policy advocacy for changes in policies hampering demand	• Training programmes • Other capacity-building support (e.g. assistance in obtaining a certification) • Financial incentives or financial support provided to suppliers • Support clustering or development of local business associations • Policy advocacy for changes in policies hampering supply	• Organising matchmaking events, site visits, and workshops • Keeping a database of local suppliers and providing MNEs with information on local firms • Provision of tailored services (e.g. guarantee recovery for delayed payments) or policy advocacy for changes in policies hampering interaction (e.g. administrative simplification, etc.)

Source: Authors' elaboration based on OECD (2015), ODI (2002), UNCTAD (2001).

The challenge of bribery and other forms of unfair treatment of business

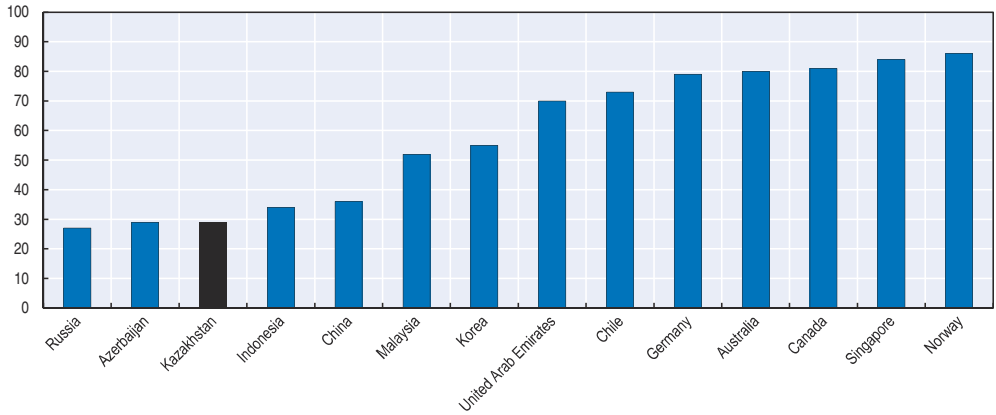
Many of the reforms described in the present chapter illustrate a willingness on the part of the Kazakh government to further improve the enabling environment for investment and to take practical measures to address it. Not surprisingly, as noted earlier in this chapter, Kazakhstan was in 2016 among the top 10 economies among 190 economies surveyed showing the most improvement in the World Bank's 2017 *Doing Business* report. The average distance to frontier (the distance to frontier is the absolute distance to the best regulatory practices) across all indicators has constantly improved since the 2012 *Investment Policy Review* of Kazakhstan.

The country has also significantly improved its ranking in the World Economic Forum's *Global Competiveness Index* in 2015-16 compared to the 2011-12 Report (up from 72 to 42 out of 140 countries).[50] However, these developments and on-going reforms aimed at further improving Kazakhstan's investment climate represent only a small part of a larger picture. As noted throughout the present *Review*, feedback from domestic and foreign enterprises indicates that the overall business environment in Kazakhstan continues to be weakened by bribery, favouritism and weak rule of law. Kazakh firms as well as foreign investors, in particular those from OECD countries but also from other countries such as Russia, most frequently mention bribery as one of the constraints in doing business.[51]

Perception of bribery and other forms of unfair treatment of business has continued to characterise the past 5 years since the first *Investment Policy Review* was undertaken by the OECD. According to various national and international reports, corruption remains a persistent national problem, although such reports recognise that Kazakhstan has made progress in its anti-corruption efforts. The level of perception of corruption in Kazakhstan is well documented.[52] According to Transparency International's annual *Corruption Perception Index* (CPI), whereas Kazakhstan occupied the 105th place among 178 countries surveyed in 2010, its score was 140th among 177 countries in 2013, and 123rd among 167 countries in 2015. During the period 2012-15, Kazakhstan had an average score of 26 on a scale from 0 (the highest level of corruption perception) to 100 (the lowest level of corruption perception) (see Figure 5.6). According to the *Global Corruption Barometer* survey commissioned by Transparency International covering the period from September 2012 to March 2013, 34 % of Kazakh citizens believed that corruption had increased "significantly" during that period, while another 45% were of the opinion that the level of corruption had not changed. One third of respondents reported they had given bribes to receive government services in the recent past.[53]

Figure 5.6. **Perception of Corruption in Kazakhstan, 2014**

Index from 0 (highly corrupt) to 100 (very clean), 2014



Source: OECD (2016), *Multi-dimensional Review of Kazakhstan: Volume 1. Initial Assessment*, OECD Publishing, Paris.

StatLink http://dx.doi.org/10.1787/888933452931

This type of pressure has reportedly affected first of all medium-sized companies. Corruption and other forms of pressure on businesses have nevertheless stymied larger domestic companies and foreign investors as well. During the past few years, bribery has primarily taken the form of facilitation payments, i.e. bribes or unofficial payments of a rather small amount.[54] Foreign investors and domestic entrepreneurs have also complained about other problems that have arisen at the interface between companies and public authorities: arbitrary and excessive inspections by local and national tax and financial authorities; unfair regulatory compliance in areas such as housing and land registration; excessive (illicit) fees in relation to licensing; non-enforcement of prescribed rules.[55]

Favouritism and political connections have also been identified as undermining Kazakhstan's investment climate. As already noted in Chapter 2, SOEs represent a large part of Kazakhstan's economy, with the SOE sector dominated by a few national holding companies such as the National Welfare Fund Samruk-Kazyna aggregating SOEs operating in different economic sectors. The management of these companies is often appointed at the political level and it has extensive links to the public sector, including access to public funding from state-owned banks as well as credit facilities. State-owned enterprises also have an advantageous position in terms of licensing. Consequently, in 2014, the OECD called for sufficient accountability and transparency in these companies and emphasized the importance of external monitoring of their operations (OECD 2014c).

Addressing business concerns

Over the past years, a vast array of mechanisms, tools and methods have been developed by the Kazakh authorities to alleviate some of the challenges that have resulted from bribe demands and other kinds of unfair treatment of businesses.[56] The government has in particular identified control of corruption as one of the key priorities in the strategy *Kazakhstan 2050*. With the goal of making more effective the fight against corruption, a new "Anti-Corruption Strategy of the Republic of Kazakhstan for 2015-2025" was approved at the end of 2014 as part of the action plan to implement the *Kazakhstan 2050* strategy.[57] The anti-corruption strategy stipulates that all state bodies and officials must strive against corruption within their area of responsibility and includes a set of new measures to fight corruption in Kazakhstan by: developing and nurturing a culture of integrity among public officials through the provision of standards of conduct and rules requiring financial asset disclosure; promoting business ethics in the private sector; reforming the judiciary; involving the participation of the civil society and the public in the fight against corruption; creating a feedback system for improvement of the anti-corruption strategy; and other measures.

Preventing misconduct in the public and private sectors

The Kazakh authorities have turned to different methods to alleviate some of the challenges that result from bribe demands. One has been to criminalise different forms of bribe payments to domestic public officials. Other ways to target the demand-side origins of bribes have involved the initiation of confiscation or forfeiture proceedings to recover property derived from corruption and the development of anti-money laundering measures to improve detection of criminal activity by law enforcement and regulatory authorities. Progress on the implementation of criminal legislation has nevertheless been mixed. In the third round of monitoring of the Istanbul Action Plan, it was noted that while Kazakhstan has taken steps forward in the area of anti-bribery policy, there has, on the whole, been a lack of progress in the areas of enforcement of criminal legislation (OECD, 2015d). In 2012, the OECD had already advocated stronger law enforcement (OECD, 2012a).

More recently, as an additional tool to reduce bribe demands, the authorities have launched new initiatives to strengthen the integrity of public service. Setting principles and standards of conduct for public officials through codes of ethics has been one way in which this has been carried out. Requiring financial asset disclosure for certain categories of public officials is another method the government has turned to. As from 2017, the new Law on Corruption Countermeasures, enacted on 1 January 2016,[58] requires all state officials (and their spouses), as well as candidates to the President, members

of Parliament and of local representative bodies (*maslikhats*) and heads of local executive bodies, to regularly disclose information about their assets and liabilities.[59] The law also contains provisions aimed at avoiding or managing conflict of interest, establishing a system that requires certain categories of public officials to disclose conflicting interests. If a side activity creates the conflict, the official may be suspended from performance of the functions that constitute the conflict or be required to change his/her position.

The government has also recently turned to programmes to help businesses resist bribe solicitation and thus ensure their contribution to Kazakhstan's anti-corruption efforts. A significant development that took place is the recent adoption of an "Anti-Corruption Charter" for businesses. Adopted in June 2016 by the National Chamber of Entrepreneurs – an umbrella organisation which brings together all commercial legal entities and individual entrepreneurs registered or recorded in Kazakhstan as well as the government of Kazakhstan –,[60] it is open for signing by all companies regardless of their place of registration and industry. Although signing the Charter is voluntary, it provides a model for prevention as it introduces to the business community general features of an effective anti-corruption programme. In particular, the Charter recognises the importance for companies to have programmes or measures for preventing and detecting corruption in their business operations in line with the principles contained in Chapter VII of the OECD *Guidelines for Multinational Enterprises* (see also Chapter 7).

Enhancing integrity and effectiveness of public procurements

Kazakhstan has also progressively taken measures to address bribery in public procurement because of the heightened risks at this major interface between the public and private sectors. The continuous adoption of amendments to the legal and regulatory framework governing public procurement during the past years illustrates this trend. Public procurement is a key activity of Kazakhstan's SOEs and also one of the largest government spending, accounting for around 43% of governmental expenses in 2010 (United Nations Economic and Social Commission for Asia and the Pacific, 2014). As acknowledged in the Anti-Corruption Strategy for 2015-2025, high levels of corruption in public procurement have characterised the past years. Businessmen have complained in particular about collusion, i.e. that technical specifications of tender documents were very often adjusted to particular suppliers.

To keep corruption at bay, and with the view to improving the business environment in Kazakhstan, steps have been taken to substantially modernise procurement. On 1 January 2016, a new law on Public Procurement, designed to facilitate and streamline the government procurement procedures and address corruption risks, came into force.[61] The new law is an improvement

compared to its predecessor as it is based on the principles of equality, free competition, non-discrimination and the independence of the supplier vis-à-vis the public buyer (OECD, 2016c). The law also contains several provisions aimed at upholding the principles of transparency and procedural fairness.[62] As compared to previous legislation dating back to 2007, the law has also broadened the scope of application and reduced the number of exemptions from the public procurement regulations. This process has gone hand in hand with some streamlining of available appeal mechanisms for the oversight of the procurement process and the introduction of a monitoring mechanism to foster integrity. However, Kazakhstan's public procurement system continues to suffer from an abundance of exceptions regulated in bylaws or ministerial orders that minimise the reach of the well-meaning new public procurement law. In particular, as already noted in Chapter 2, state-owned enterprises can organise purchases according to their own rules.

The government has also been increasing efforts to render electronic public bidding proceedings and make them accessible through the web. In 2010, Kazakhstan launched its electronic Government Procurement (e-GP) system with a view to improving and facilitating transparency (OECD, 2016a). Since then, the legislation specifies that public procurement processes should be conducted through the e-procurement portal (*goszakup.gov.kz/*) to minimize interaction between officials and potential bidders, thereby reducing bidders' vulnerability towards bribe solicitation.[63] International organisations such as the Asian Development Bank have reported that procurement in Kazakhstan now is largely executed through the electronic government procurement web portal launched in 2010.[64] It nevertheless remains unclear what proportion of all government contracts are covered by the law. Also, as noted above, procurements of state-owned enterprises are not covered by the law and therefore it is likely that Kazakhstan's e-procurement system does not apply to them.

Reforming the judiciary

As a response to the perception of weak rule of law and lack of professionalism in the judiciary judicial reform has been underway with the overall objective to strengthen foreign and domestic investors' trust in Kazakhstan's courts. Amendments were introduced in 2015 to the Law on Judicial System, with new rules that apply to the selection and disciplining of judges.[65] The measures include toughening qualification criteria for the recruitment of judges by introducing a new requirement for a candidate to serve at least five years within the court system (or at least ten years as a lawyer) and a one-year trial period for newly appointed judges.[66] Higher level judges are required to have lower court experience. The law, as amended, also provides for the establishment of an Academy of Justice for the purposes of professional advancement and training of judges. The professional activity of

each judge (except judges with more than 20 years of judicial experience) will also now be assessed by a Court Jury every five years.[67] Steps to increase the liability of judges for breaches of ethical standards and violations of the legislation have also been taken with the adoption in October 2016 of a new Code of Judicial Ethics, replacing the one dating from 2009.

In order to diffuse concerns about the lack of professionalism and independence of the judiciary, on 1 January 2016 a new Law on Supreme Judicial Council, replacing the previous one on the same subject, came into force.[68] The law allegedly targets the independence and composition of the Supreme Judicial Council which, under Kazakh law, gives recommendations on the appointments of magistrates (judges are appointed by the President of Kazakhstan upon recommendations made by the Council). Membership in the Council has been broadened through inclusion of new state bodies; civil society representatives may become members of the Council upon the President's decision. The independence of the Council from undue interferences is stipulated in the law.

Kazakhstan has taken additional steps to strengthen the performance of its justice system, by developing mechanisms tailored specifically to businesses' legal needs. As seen in Chapter 3, this includes the establishment of a dedicated panel of judges at the court of Astana to hear investment disputes and new alternative dispute resolution mechanisms.

Providing channels of communication to companies to resist unfair treatment

These measures have gone hand in hand with the establishment of dedicated bodies to facilitate communication and consultation with investors, provide a channel to relay investors' concerns to relevant governmental agencies, thus potentially influencing government activities, decisions, behaviour, regulations having an impact on the investment climate. Illustrations of this include the establishment of government-sponsored councils at the National Chamber of Entrepreneurs (NCE) of the Republic of Kazakhstan – the Council for Fighting Corruption and the Shadow Economy and the Council for the Protection of the Rights of Entrepreneurs – as well as the recently-established Commissioner for Protection of Entrepreneurs Rights (hereafter: the Business Ombudsman), also housed in the Chamber.

The National Chamber of Entrepreneurs' Council for Combating Corruption has been operating since 2014.[69] In addition to senior officials of the Chamber itself, it consists of accredited associations, representatives of government authorities – including officials of the Ministry for Investments and Development –, and members of parliament and the media. The Council's primary purpose is to provide for the practical participation of businesses in

Kazakhstan's anti-corruption efforts. In 2014 as well, still within the Chamber, a Council for the Protection of the Rights of Entrepreneurs – bringing together parliamentary and civil society representatives, representatives of government agencies and state bodies, Kazakhstan's business community, and experts in the field of law – was established to examine and resolve claims of entrepreneurs related to situations of corruption and other forms of administrative and legal abuse by state and local authorities. In April 2016, the Council was processing over 11,500 complaints coming from all regions of Kazakhstan.[70] Breaches by public officials which give rise to criminal liability are referred to law enforcement authorities in the framework of co-operation agreements (memoranda of understanding) that have been signed with the General Prosecutor's Office and the prosecutor's office in all regions as well as in the cities of Almaty and Astana.

Still recently, following the examples of other countries in the region and beyond such as Georgia, Korea, the Russian Federation and Ukraine, Kazakhstan has stepped up its efforts to enhance dialogue with investors to alleviate some of the challenges that result from bribe and other illegal demands on businesses through the establishment of two dedicated Ombudsmen: one is called the Investment Ombudsman; the other is called the Commissioner for Protection of Entrepreneurs Rights (or Business Ombudsman).[71] Both have been designed to address instances of unfair treatment of businesses by public officials; to quickly provide remedies; and, based on an assessment of complains addressed to them, to make proposals to the government on how to improve the business climate in Kazakhstan, including proposals to amend legislation and regulations (Box 5.14 below). The Investment Ombudsman has been operating

Box 5.14. **Main characteristics of the Investment Ombudsman and the Commissioner for Protection of Entrepreneurs Rights (the Business Ombudsman)**

There are many similarities between the Investment Ombudsman and the Commissioner for Protection of Entrepreneurs Rights (the Business Ombudsman).

Functionally, both institutions have been designed to address instances of unfair treatment of businesses by public officials. As a result, both ombudsmen have been empowered to receive complaints of unfair practices against companies in addition to bribery such as repetitive tax audits, excessive licensing fees, threats, retaliation or other unfair regulatory enforcement actions by Kazakhstan's public agencies.

Both are intended to be incidental to other anti-corruption efforts undertaken by the government in general and by specific state and local agencies. They are not intended to undermine existing legal processes but rather to complement them by providing an avenue to those companies that

Box 5.14. **Main characteristics of the Investment Ombudsman and the Commissioner for Protection of Entrepreneurs Rights (the Business Ombudsman)** *(cont.)*

seek a more informal platform through which to address their grievances and obtain, whenever possible, a speedy response to resolve issues. In short, they are not judicial tools, although both institutions may pass reports to law enforcement authorities where there are reasonable grounds to suspect a violation of the law. The Business Ombudsman may also file a lawsuit in court.

Both mechanisms rely on a kind of third party – the Investment Ombudsman at the Ministry for Investments and Development; the Business Ombudsman at the National Chamber of Entrepreneurs – who plays the role of being the facilitator between the complainant and the concerned public agencies. Both have access to relevant information in the possession of government bodies and officials and powers to make recommendations to such bodies and officials. At the same time, the mandate of both mechanisms – along the lines of similar institutions established in other countries – exclude the authority to exercise enforcement actions, including prosecution powers. Also, neither of the two ombudsmen has the power to override the illegal acts of other public agencies or to compel compliance with any recommendations.

Last but not least, both mechanisms also encompass an advisory role to the government. For example, the Investment Ombudsman is empowered to develop and submit to the government recommendations on improving legislation aimed at enhancing the investment climate. Both Ombudsmen are accountable to the executive branch of government: the Investment Ombudsman is appointed by and report to the Prime Minister; the Business Ombudsman is appointed and report to the President.

There are also differences. The structure and composition of Kazakhstan's Investment Ombudsman is perhaps the most visible difference compared to the Business Ombudsman. Organisationally, the Investment Ombudsman functions are carried out by the Minister for Investments and Development of Kazakhstan, whereas the Business Ombudsman is housed in the National Chamber of Entrepreneurs; a separate secretariat, not formally rooted in government, supports the latter. There are also differences in the mandate accorded to each institution. Only the Business Ombudsman institution contemplates the right to publicly reports about the complaints it has handled and the way in which it has handled them. The Business Ombudsman has also its own website (*http://ombudsmanbiz.kz/eng/*) which publicises the mechanism and also allows the complainants to submit a complaint online.

since 2014. From its date of inception to the first quarter of 2016 the mechanism received some 150 complaints; out of 62 complaints received in 2015, 20 decisions had been solved in favour of investors.[72] On its part, the Business Ombudsman institution was established in 2016. At the time of writing (third quarter of 2016), the institution had received 40 complaints; out of which 29 were under consideration (11 had been solved).[73]

Going beyond reforms

Many of these recent reforms illustrate a willingness on the part of the Kazakh authorities to acknowledge the problem of bribery and other forms of unfair practices in Kazakhstan and to take practical measures to confront them. This appears to be a worthwhile goal, which in time could have a direct influence on the perception of the investment climate. Legal and business representatives met by the OECD Secretariat in the framework of this *Review* seemed for example hopeful that the judicial environment was improving. They also cited an increasing amount of communication on corruption matters between the Kazakh authorities and the private sector through the above-mentioned government-sponsored working groups and councils.

Notwithstanding such developments, the real impact of the various measures described above remains to be seen. Past reforms have been closely monitored under the Istanbul Action Plan. In 2015, while recognising that Kazakhstan had taken steps forward in the area of anti-corruption policy, the OECD Anti-Corruption Network for Eastern Europe and Central Asia (ACN) noted there was still a clear weakness in translating these intentions into results (OECD, 2015d). The government appears to be committed to cleansing the system of corruption. New laws have been enacted; the authorities have prepared the necessary action plans and programmes. However, the real test can only be met through determined implementation of actions on the ground every day. For example, while the adoption of an Anti-Corruption Business Charter is an important step to encourage the development of preventive measures among the business sector, the impact will be felt only if both the government and Kazakhstan's leading business association make efforts to promote the Charter through awareness-raising and training programmes. In this regard, Kazakhstan could make use of the OECD *Good Practice Guidance on Internal Controls, Ethics and Compliance*. Although directed at foreign bribery, the *Guidance* can be a useful reference for designing and implementing a strong corporate compliance programme.

Furthermore, there are questions as to whether the recently adopted reforms would fully meet the objectives officially set by the President. Despite reforms in the judiciary, there is still limited separation of powers as the Supreme Court and local courts, as well as members of the Supreme Judicial

Council, are appointed by the President. Many exceptions apply to the recently introduced regulations on conduct in office and conflicts of interest as well as to the duties to report on assets and liabilities. A credible checking mechanism for assets declaration as well as effective sanctions in case of false or inaccurate declarations are also lacking.

Although the changes in the legislation governing public procurement would appear to represent progress with respect to efficiency, transparency and procedural fairness, their impact is yet to be seen. Moreover, although the number of possible exceptions to publically open procurement procedures has decreased since the enactment of the new public procurement law, they remain numerous. As noted above, for example, state-owned enterprises are not subject to the public procurement law and can organise purchases according to their own rules. Kazakhstan's sovereign wealth fund Samruk Kazyna, Kazakhstan's largest purchaser which procures a considerable share of the infrastructure projects in the country, does not operate under the law on public procurement either. One of the main areas for further reform should be to increase the share of procurement processes managed under the rules of the public procurement law. The legislation is also far from being aligned with international standards. One of the government's priorities should be to effectively combat collusion in public procurement to level the playing field for suppliers and allow them to do business with the public sector on a fairer basis. The OECD *Recommendation on Fighting Bid Rigging in Public Procurement* could be useful in this regard as it supports close co-operation between competition and contracting authorities to identify markets in which bid rigging is more likely to occur and for which special precautions should be taken.

While foreign investors have access to new redress mechanisms, it is difficult to ascertain at this early stage to which extent the establishment of these reporting mechanisms has added values to the fight against bribery and other forms of abuse by state and local agencies and exactly which results these mechanisms have produced. For example, businesses met in the context of the present *Review* complained that the post of the Investment Ombudsman has remained largely ineffective so far. Clear responsibility and coordination between these bodies in their efforts to facilitate the handling of complaints by corporations affected by public authorities' activities is also key to effective implementation of Kazakhstan's anti-corruption strategy. The overlap of the functions between the Entrepreneurs' Rights Commissioner, the Investment Ombudsman and the Protection of the Rights of Entrepreneurs' Council should be avoided. The multiplicity of actors may also generate confusion among investors.

In addition, as the experiences of Colombia's High Level Reporting Mechanism and Ukraine's Business Ombudsman Council prove, such mechanisms can only be successful if they are seen to be sufficiently impartial

in companies' eyes (Wehrlé, 2015). There is a possible downside of Kazakhstan's choice to locate its Investment Ombudsman in the Ministry for Investments and Development. For sure, one could argue that the merits of the Ombudsman lie in being housed in the ministry, which include access to other government institutions for the purpose of obtaining information and better coordination among agencies and ministries. At the same time, the Ombudsman might not be seen independent enough from the government. Similarly, much of the credibility of the Entrepreneurs' Rights Commissioner is tied to the degree of credibility of the National Chamber of Commerce. The latter has been perceived by foreign investors as well as by international institutions as being too much tied up with the branches of government in Kazakhstan (president, council of ministers, and parliament) as well as state-owned businesses.[74] The recent experience of Ukraine's Business Ombudsman Council, which is neither a constituent part of the hierarchy of authority nor accountable to any branch of government, can be useful in this regard (OECD, 2016b).[75] Korea's Foreign Investment Ombudsman also provides a good example of trusted grievance resolution mechanisms.

Policy recommendations

Kazakhstan is currently undergoing major administrative reforms aimed at facilitating and promoting investment. They have been launched in recognition that administrative simplification, the use of one-stop shops and specific tools that ensure a proper consideration of investors' concerns during the early stages of policy-making can translate into increased investment. With a strong focus on administrative streamlining, these reforms may however miss the primary source of overlapping and conflicting administrative requirements, i.e. poor-quality legislation. Furthermore, these developments represent only a small part of a larger picture. The overall business environment continues to be weakened by bribery, favouritism and weak rule of law. The need to enhance the fight against bribery and other forms of abuse on entrepreneurs is a crucial challenge for Kazakhstan. Properly addressing business concerns in these areas requires determined implementation of several reforms.

Investment facilitation

- *Ensure that business views are taken into account in the design of future investment facilitation reforms:* To-date many reforms in the area of investment facilitation in Kazakhstan have been driven by the desire to improve the country's *Doing Business* rankings. In order to ensure that future reforms address adequately business needs, it is critical that the government seeks regular feedback from investors – not only large foreign investors – on the

obstacles to doing business. The Investment Committee of MID or Kaznex Invest can play a useful role in this regard.

- *Ensure that the business community is aware of the functioning of the one-stop-shop (OSS) for business registration:* The OSS was launched in pilot form in 2015, applying to strategic investment projects only, and extended to all firms in 2016. As the government operationalises the OSS, it should ensure that the business community is familiar with the services provided as well as provides the authorities with feedback as to the features that could be extended or improved.
- *Improve transparency of the process of creating new laws and regulations:* Multiple, speedily-passed laws with conflicting or insufficiently defined requirements complicate the interpretation of administrative rules by firms and leave scope for arbitrary interpretation by the authorities, offering a breeding ground for corruption. Respecting advance notice requirements and involving a broad base of stakeholders in the *ex-ante* consultation process can help improve the status quo.

Investment promotion

- *Define a clear investment promotion strategy that would outline the goals and tools of investment promotion strategy in Kazakhstan*. While in the past, the government used four year investment promotion plans linked to the country's economic development plan (SPAIID and Vision 2050), it appears that no such plan currently exists. Best practices suggest that such strategy should be easily available to on-line, outlining clearly government's goals.
- *Clearly define responsibilities and agree on modes of co-operation between different agencies involved in investment promotion activities in Kazakhstan*. While Kaznex Invest serves as the national Investment Promotion Agency in Kazakhstan, several other agencies perform investment promotion activities. In order to avoid a waste of resources and ensure complementarity, some of their functions could be streamlined or resources and facilitates shared.
- *Improve the efficiency of Kaznex Invest and reorient its functions towards serving investors, not other government bodies:* As Kaznex Invest matures as an organisation, it would be advisable that it learns from best practices in other countries to increase its effectiveness, currently evaluated as low, and engages in a full range of investment promotion activities, including aftercare services, organisation of SME-MNE linkage formation programmes and policy advocacy.

Addressing bribery and other forms of wrongdoing by public agencies and entities

- *Implement determinately anti-bribery and integrity measures,* notably in the areas highlighted by the third round monitoring report on Kazakhstan under the

Istanbul Anti-Corruption Action Plan and by the Integrity Scan of Kazakhstan undertaken under the auspices of the OECD CleanGovBiz Initiative.

- *Promote effective safeguards to increase transparency and fight bribery in civil service*, notably through the development of efficient systems that proscribe conflicts of interests in line with the OECD *Recommendation on Guidelines for Managing Conflict of Interest in the Public Service*.
- *Further modernise justice institutions* with the objective to improve their integrity and independence.
- *Develop an appropriate public procurement system* in line with the OECD *Recommendations on Public Procurement* and *on Fighting Bid Rigging in Public Procurement*, especially in terms of transparency and accountability, oversight, and fair and equitable treatment for potential suppliers.

Notes

1. Article 28 of the Law No. 202-V "On Permits and Notification" of 16 May 2014.
2. The legal basis for the OSS is enshrined in Article 282 of Entrepreneurial Code of RK No. 375-V dated 29 October 2015.
3. Two recent studies – Corcoran and Gillanders (2012) and Jayasuriya (2011) – find a small significant effect, driven primarily by the "trading across borders" indicator.
4. For example, Bénassy-Quéré et al. (2007) find a positive impact of the quality of institutions on inward FDI independently of GDP per capita; Zhang (2007), Daude and Stein (2007) show the positive impact of regulatory quality on FDI, in particular in less developed countries; and Habib and Zurawicki (2002), Egger and Winner (2006), Wei (2000) and Al Sadig (2009) find a significant negative effect of corruption.
5. At that time, the country did not then have a systematic mechanism of open public consultation on either primary or secondary legislation in place and the available methods and procedures for impact assessment were limited and not obligatory for all legal drafts (OECD, 2014).
6. The Law No. 401-v "On Access to Information" of 16 November 2015 implemented the constitutional rights of all persons to receive and disseminate information by all means not prohibited by law. According to the Law, all draft laws and regulations are required to go through "public discussions" process on the Internet portal "Open Normative Legal Acts". The Law No. 383-V "On Public Councils" of 2 November 2015 implemented the state policy on the formation of public councils. Consultations via public councils have been mandatory in Kazakhstan since 2009 (OECD, 2014).
7. Article 63 of the Entrepreneurial Code sets out the rules for engagement of accredited business associations in assessing draft laws, regulations and international treaties and the accreditation process. Accredited business associations, together with other accredited bodies, can provide their views on draft laws and regulations submitted to the Expert Council for Private Enterprise by a central or local government body for expert opinion. Article 65 specifies that the government is to send draft regulations for an expert opinion of the Council for no less than 10 working days and, when doing so, accompany the draft law with an explanatory note that contains the results of regulatory impact assessment of the proposal legal act on business. The expert advice is advisory in nature and,

according to Article 66, is "an essential supplement to the draft law concept". Article 67 of the Code also specifies that all draft normative legal acts affecting businesses are subject to mandatory publication in the media, including Internet, prior to their consideration by the appropriate body or at the meeting of the Expert Council for Private Enterprise.

8. As of 1 August 2016, the number of draft laws and regulations posted on the portal was 1853. Website was viewed 45,408 times and comments by the public were submitted on 74 out of all 1853 laws.

9. Selection criteria for public councils were also criticised as being unclear in OECD (2017, forthcoming) and OECD (2014). Kazakhstan applies a commenting period of ten working days, while OECD countries with mandatory consultations periods allow on average a period of four to six weeks. Best practices also suggest that comments obtained from stakeholders should be published and, whenever possible, commenting stakeholders should receive motivated responses as to how their suggestions were addressed (OECD, 2015b).

10. See Article 65 and 82-83 of the Entrepreneurial Code.

11. The review recommended an establishment of "a fully-fledged regulatory impact procedure when preparing regulations to capture the full consequences (benefits and costs) of draft regulations, building on the existing requirements for scientific expertise".

12. Information based on the OECD consultations with stakeholders in Kazakhstan in 2015-16.

13. Address of the President of Kazakhstan to the nation, "Kazakhstan's Way – 2050: Common aim, common interests, common future", 17 January 2014.

14. Decree of the President No. 992 "On Strategic development plan of the Republic of Kazakhstan till 2020" dated 1 February 2010.

15. Decree of the President of the Republic of Kazakhstan No. 874 dated 1 August 2014.

16. These are: ferrous and non-ferrous metallurgy; oil refining; petrochemical industry; food production; agro-chemistry; production of chemicals for industry; manufacture of vehicles, spare parts, accessories and motors; electrical equipment; manufacture of agricultural equipment; railway equipment manufacture; manufacture of machinery and equipment for mining industry; manufacture of machinery and equipment for oil refining and oil producing industry; construction materials production; and "innovative sectors", which are defined to mean mobile and multimedia technologies, nano- and space technology, robotics, genetic engineering, and renewable energies.

17. The Order No. 406 of the Minister for Investments and Development of 28 April 2016 approved the plan.

18. Decree No. 103 of 24 February 2016 includes a detailed plan on how to implement 12 out of the 19 recommendations made by the OECD at the time of the previous *Investment Policy Review* of Kazakhstan.

19. Information based on written answers submitted by the government of Kazakhstan in the framework of the current *Review*.

20. Decree of the President No. 992 "On Strategic development plan of the Republic of Kazakhstan till 2020" dated 1 February 2010.

21. The sectors identified as priority sectors in the Vision 2050 are: agricultural production and processing; construction industry and construction materials; oil

refining industry and infrastructure for oil projects; metallurgy and production of finished metal products; chemical, pharmaceutical and defence industries; power generation; and transport and communications sector (Government of Kazakhstan, 2010).

22. These are: ferrous and non-ferrous metallurgy; oil refining; petrochemical industry; food production; agro-chemistry; production of chemicals for industry; manufacture of vehicles, spare parts, accessories and motors; electrical equipment; manufacture of agricultural equipment; railway equipment manufacture; manufacture of machinery and equipment for mining industry; manufacture of machinery and equipment for oil refining and oil producing industry; construction materials production; and "innovative sectors", which are defined to mean mobile and multimedia technologies, nano- and space technology, robotics, genetic engineering, and renewable energies.

23. As mentioned earlier, SPAIID 2015-2019 identifies 6 priority branches (metallurgy, chemistry, petro-chemistry, mechanical engineering, material construction and food industry) divided into 14 sub-sectors (Decree of the President of RK No. 874 of 1 August 2014). The Decree of the Prime Minister of RK No. 13 of 14 January 2016 provides the actual list of sectors to be considered for priority investment projects.

24. As stipulated in Article 286 of the Code, "investment preferences are granted on the basis of an investment contract between the authorised body on investment and the legal entity of the Republic of Kazakhstan implementing an investment project."

25. Information provided by the Government of Kazakhstan.

26. As per definitions embedded in the Entrepreneurial Code, investment priority project is an investment project implemented by the newly established entity (i.e. the state registration of such a legal entity needs to have been completed no earlier than 24 months before filing of an application for the investment incentive) under the identified priority activities with the amount of investment above the pre-identified threshold. The allocation of incentives is also subject to compliance with other conditions in paragraph 282 of the Entrepreneurial Code.

27. Chapter 8 "State Support of Private Enterprises" of the Entrepreneurial Code of RK No. 375-V dated 29 October 2015.

28. For a full overview of all available financial support instruments, see Government of Kazakhstan (2014: 114-117).

29. The recent creation of the Commission for Industrial Development and the National Institute for Industry Development was supposed to facilitate better monitoring and co-ordination (Government of Kazakhstan, 2014; OECD, 2016: 143).

30. The implementation of the program was supported by the Asian Development Bank (ADB), based on a framework agreement on co-financing signed in May 2014.

31. For example, while SMEs contribution to GDP is about 25% in Kazakhstan, the corresponding shares in such OECD countries as Poland and Turkey are 47% and 59%, respectively. The share of population employed in the SME sector in Kazakhstan (of 26-30% in the past five years) is also much lower than in many OECD countries, such as the United States and Turkey, where it reaches 54% and 81%, respectively. Also, even though in January 2014 the number of registered small enterprises (small companies, individual entrepreneurs, and farmers) reached 1.5 million, only 56.4% were economically active and over two thirds were in the form of individual entrepreneurship without the creation of a legal entity (World Bank, 2015b).

32. See, for example, Khakimzhanov and Seitenova (2013) for an overview and assessment of Kazakhstan's industrial policies planning and implementation.

33. The programme has been approved by Decree of the Government of Kazakhstan No. 168 dated 31 March 2015.

34. The goals of the national cluster policy have been outlined in the Concept for formation of the prospective national clusters in Kazakhstan till 2020, approved by the Government Decree No. 1092 dated 11 October 2013.

35. They are primarily regulated by the Law No. 469-IV "On Special Economic Zones in the Republic of Kazakhstan" of 21 July 2011, most recently amended in 2014 and 2015.

36. The amendments to the Law on SEZs were passed 27 October 2015.

37. See WTO (2015a, §0933).

38. See WTO (2015a, §0934). Following that date, the goods of juridical persons which had been registered and active in SEZs and free warehouses prior to Kazakhstan's accession to the WTO would continue to enjoy the treatment with respect to local content requirements, sufficient processing, and exemptions from tariffs and taxes (WTO, 2015a: §0934). In addition, goods imported into free warehouses and SEZs under provisions that exempt imports from non-EAEU Members from customs duties and certain taxes, would be subject to those duties and taxes and customs formalities when released to the rest of the territory of Kazakhstan and the territory of the EAEU; and if those imported goods were substantially transformed within the territory of an SEZ or in a free warehouse, the duties and taxes that would otherwise have been assessed for those goods are to be paid when the final products enter the rest of the territory of Kazakhstan and the territory of the EAEU. See WTO (2015a: §0896).

39. See WTO (2015a: §0585). Relevant subsidies are specified in Table 4 in WTO (2015a). It was also confirmed that Kazakhstan would not invoke any of the provisions of Articles 27 and 28 of the SCM Agreement, which relate to exceptions and transition periods in the application of the SCM Agreement available to developing countries. See (WTO 2015a: §0585)

40. In addition, the IPA's legal status and reporting structure as well as the quality of the materials it presents on its website is also found to impact the volume of the FDI attracted (Harding and Javorcik 2007, 2011). In particular, subunits of ministries are found to be less effective in attracting FDI than agencies with a more autonomous status and accountability to an external entity positively affect agencies' performance. This confirms some of the earlier case study findings (Wells and Wint, 2000) and complements a cross-country study by Morisset and Andrews-Johnson (2004), which demonstrates that, on average, the IPA's budget is positively correlated with increase in FDI flows, once the per capita income and the quality of investment climate are controlled for.

41. For example, the National Institute for Technological Development has several relevant functions in the area of attracting and promoting investment in technology-intensive activities; the National Institute for Industrial Development supports the planning of the national cluster policy; and the National Institute for Local Content creates and maintains a database of local suppliers and helps promote the use of local content. See Article 246 §4 of the Entrepreneurial Code.

42. According to the government, the Council has offices in more than 70 countries.

43. United States (Washington), Germany (Berlin), France (Paris), China (Beijing), UK (London), Italy (Rome), South Korea (Seoul), Iran (Tehran), Japan (Tokyo), India (Delhi).

44. United States (New York), Germany (Frankfurt), Turkey (Istanbul), UAE (Dubai), China (Beijing).

45. E.g. the IPA of Netherlands has 27 foreign offices and UKTI professional advisers in over 100 countries.

46. In 2014, the government adopted five national investment priority industries to be promoted by Austrade, which are listed on Austrade's website, and towards which the agency is mandated to attract investment into.

47. e.g. National Institute for Industrial Development charged with developing inputs into national cluster policy and a map of enterprises in different regions, and could also provide relevant inputs.

48. The ILP was created in 1996 to allow both local suppliers and large buyers to benefit from income tax reductions when they contribute to building productive capacity of local firms and improving the quality of their services. 906 SMEs were registered under the ILP by 2007, with 128 supplying to MNEs or large companies. The sectors vary, but one of the most recent successes of the ILP was the increased sourcing of global supermarket, such as Tesco, from local food processors (OECD, 2013: 145).

49. In Singapore, the Economic Development Board (EDB) organised supplier development programmes whereby a manager in a foreign firm was paid by the EDB to select and develop local suppliers. 32 partnerships were formed between 1986 and 1994 involving 180 domestic suppliers. Productivity of suppliers rose by 17% already in first stages of the project. In Ireland, the country's Industrial Development Agency (IDA) led a consortium of agencies that identified potential linkages in a range of sectors, developed a group of domestic suppliers, and offered buyer support and development services. Between 1985 and 1992, foreign affiliate increased their local purchases of raw materials by half and their purchases of services by one third (World Bank, 2005: 172).

50. Kazakhstan is currently undergoing an OECD review of its innovation system (OECD, 2016, forthcoming).

51. The World Economic Forum (2016), *The Global Competitiveness Index 2015-2016*.

52. American Chamber of Commerce in Kazakhstan, *Improving Kazakhstan's Investment Climate: Top Ten Barriers to Foreign Investment*, Amcham White Paper May 2014; *Ernst & Young's Attractiveness Survey: Kazakhstan 2014* (Ernst & Young, 2014), p.20; Survey of representatives of over 100 Russian companies operating in Kazakhstan in Dossym Satpayev, *Corruption in Kazakhstan and the Quality of Governance*, *IDE Discussion Paper* No. 475, August 2014, p.22.

53. In addition to international organisations, domestic civil society and business organisations, such as the National Chamber of Entrepreneurs of Kazakhstan, the Sange Research Centre and Transparency Kazakhstan, regularly conduct independent research on corruption in the country. The now defunct Financial Police Agency (reorganised in March 2015 into a state body to report directly to the president) also periodically conducted sectoral studies of corruption risks. Other government institutions have regularly conducted surveys of corruption prone areas. The print media also regularly expose public corruption and government abuses of authority.

54. Transparency International, *Global Corruption Barometer* 2013.

55. Facilitation payments are payments made to induce public officials to perform their functions, such as issuing licenses or permits (see the OECD *Convention on Combatting Bribery of Foreign Public Officials in International Business Transactions*). For example, according to media reports, in 2011 a subsidiary of a major British catering

and services company established in Kazakhstan would have made small facilitation payments to the country's customs officials in order to release goods from customs (*The Guardian*, 22 June 2015). From 2003 to 2005, a Kazakh subsidiary of Pride International Inc., which owns and operates oil and gas drilling rigs throughout the world, allegedly paid bribes totalling USD 364 000 through a freight forwarding agent and a tax consultant to Kazakh government officials to reduce customs-related penalties and taxes, and to otherwise obtain favourable customs treatment (source: U.S. Securities and Exchange Commission (SEC) Digest Numbers D-86, D-85, D-84, and D-83).

56. American Chamber of Commerce in Kazakhstan, *Op. cit.;* "Doing Business in Kazakhstan", United States Diplomatic Mission to Kazakhstan website, *http://kazakhstan.usembassy.gov*; "2015 Investment Climate Statement- Kazakhstan", US Department of State website, *www.state.gov;* "Gani Kasymov: "It is important to create the most favourable conditions for the preservation of business", Atameken (National Chamber of Entrepreneurs of the Republic of Kazakhstan) website *http://almaty.palata.kz/en/news/22238; information collected by the Ministry for Investments and Development on the basis of complaints addressed to the Investment Ombudsman*.

57. For a comprehensive account of Kazakhstan's anti-corruption policies up to 2015: OECD Anti-Corruption Network for Eastern Europe and Central Asia (ACN), "Anti-Corruption Reforms in Kazakhstan. Round 3 Monitoring of the Istanbul Anti-Corruption Action Plan (October 2014); Istanbul Anti-Corruption Plan, "Third Round Monitoring. Progress Updates: Kazakhstan", 15th ACN Istanbul Action Plan Meeting on 23-24 March 2015.

58. The Anti-Corruption Strategy was approved by presidential decree No. 986 dated 26 December 2014.

59. Law of the Republic of Kazakhstan No. 410-V dated 18 November 2015 "On Corruption Countermeasures".

60. As from January 2020, certain information will be made available to the public.

61. Membership in the National Chamber is compulsory for everyone engaged in business in Kazakhstan. The Charter is the result of work undertaken by the Chamber's Council for Combating Corruption, whose mandate is to provide for the practical participation of businesses in Kazakhstan's anti-corruption efforts.

62. Law "On Public Procurement" adopted on 4 December 2015, complemented by the new "Public Procurement Rules" approved on 11 December 2015.

63. For example the new law provides that 10 days prior a tender, technical specification will be publicly available and the public will have the opportunity to submit comments.

64. In addition, the Law "On Public Procurement" adopted on 4 December 2015 foresees the conclusion of contracts in electronic format via the e-procurement portal.

65. Asian Development Bank, "Sector Assessment (summary): Public Sector Management", Countercyclical Support (RRP KAZ 49083).

66. Constitutional Law of the Republic of Kazakhstan "On Amendments and Additions to Constitutional Law of the Republic of Kazakhstan "On the Judicial System and Status of Judges dated 25 December 2000 No. 132-II".

67. Previously, two years of working experience was enough to become a candidate for a judge.

68. A Court Jury is a special commission consisting of experienced judges for the purposes of judges' professional activity assessment as well as for consideration of judges' resignation and disciplinary liability issues.

69. Law of the Republic of Kazakhstan dated 4 December 2015 No. 436-V "On the Supreme Judicial Council of the Republic of Kazakhstan".

70. The Council was established by the order No. 81 of the Chairman of the Board of NCE "On the establishment of the Council on Fighting Corruption and the Shadow Economy at the National Entrepreneurs of the Republic of Kazakhstan 'Atameken'" dated 9 April 2014, as amended by the order No. 95 dated 27 April 2016.

71. Source: Website of the National Chamber of Entrepreneurs of the Republic of Kazakhstan 'Atameken', 7 April 2016, accessed on 21 June 2016: *almaty.palata.kz/en/news/22238*. Complains from the capital city of Astana accounted to only 9% of the total number of complaints submitted to the Chamber.

72. Both institutions are regulated under Chapter 28 of the Entrepreneurial Code of the Republic of Kazakhstan No. 375-V of 29 October 2015.

73. Data provided by the Government of Kazakhstan (June and September 2016) and statistical data displayed on the Ministry for Investments and Development website (accessed on 9 August 2016): *http://invest.mid.gov.kz/en/news/2015-investment-ombudsman-helped-20-companies-working-kazakhstan*.

74. Data provided by the Government of Kazakhstan (June 2016).

75. American Chamber of Commerce in Kazakhstan, *Improving Kazakhstan's Investment Climate: Top Ten Barriers to Foreign Investment*, Amcham White Paper, May 2014, p. 29. In June 2016 the International Labour Organisation (ILO) urged the government to amend the provisions of the Law on the National Chamber of Entrepreneurs to ensure the full autonomy and independence of employers' organisations: See Chapter 7 on employment and industrial relations.

76. Ukraine's Business Ombudsman Council is accountable to a governing board comprising local and foreign business associations, international organisations and government representatives. See Wehrlé, F. (2015), *High Level Reporting Mechanisms in Colombia and Ukraine*, Working Paper Series No. 19, International Centre for Collective Action and OECD, Basel, Switzerland.

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Chapter 6

Trade policy and the impact of WTO entry

In 2015, after a 19-year long negotiation process, Kazakhstan joined the World Trade Organisation (WTO). The event has marked a milestone in the country's trade reform process and cemented the trade liberalisation under way. Still, to help reduce high trade costs faced by firms and overcome the geographical disadvantage related to the country's landlocked position, further reforms are necessary, in particular in the area of trade facilitation and reducing regulatory barriers to trade. Closer economic integration via deep free trade agreements (FTAs) as well as committed domestic reform and investment in infrastructure will play an important role in this process.

Kazakhstan's trade policy is another key policy area that influences its ability to attract foreign investors. Trade policy has a direct incidence on countries' investment climates by affecting the relative prices of firms' inputs and final products sold domestically and in foreign markets. This trend has accentuated even more with the spread of global value chains, where different stages of production are scattered across borders, and rely on effective trade links and cross-border coordination. Recognising the importance of an open trade policy for a conducive business climate, many countries undertook extensive trade-related policy reforms, including through reductions of import tariffs, offering import duty exemptions to certain firms, modernising their border control systems, negotiating bilateral and regional trade agreements, or otherwise facilitating trade.

Kazakhstan has also undertaken a series of important trade policy reforms since early 1990s. For example, the average level of import tariffs were lowered (from 9.5% in 1996 to 2.6% in 2004), and some investors benefitted from full exemptions from import duty payments (e.g. those operating in special economic zones and having signed investment contracts with the state). Certain restrictions on market access of foreign services operators were also reduced, even though the progress has been slower in this regard. Finally, in 2015, the country concluded its accession to the World Trade Organisation (WTO) (see Box 6.1), which marks an important step in Kazakhstan's trade reform process with implications on the overall business climate. The following section describes the reforms required by the country's WTO entry and their implications as well as highlights other trade-related reforms required to improve the investment climate.

Box 6.1. **Overview of the Kazakhstan's accession process to the World Trade Organisation (WTO)**

The Government of Kazakhstan applied for accession to the WTO on 29 January 1996. The negotiations have lasted for nearly 20 years, culminating in the formal signature of the terms of Kazakhstan's entry on 27 July 2015 in Geneva, Switzerland. Kazakhstan ratified the WTO Accession Protocol on 12 October 2015, and has officially become the 162nd member of the WTO on 30 November 2015.[1] Certain of Kazakhstan's WTO commitments came into entry at the time of its entry, while others will be implemented within a specified period of time.

Box 6.1. **Overview of the Kazakhstan's accession process to the World Trade Organisation (WTO)** *(cont.)*

Kazakhstan's WTO accession package comprises of three elements:

- Goods Schedule, summarizing the country's commitments in relation to goods
- Services Schedule, outlining the list of specific commitments relating to the services sectors
- Report of the WTO Working Party, summarizing other specific obligations that Kazakhstan committed to during the negotiation process.

Besides these three documents, by the time of its entry, Kazakhstan is also subject to the entire legal *acquis* of the WTO, to which it committed to abide to (negotiated transition periods and other exceptions notwithstanding). The compliance of Kazakhstan with the terms and conditions of its entry is subject to several monitoring and enforcement mechanisms. The most important one is the WTO Dispute Settlement Mechanism (DSM) – a system whereby one or more WTO members can submit a complaint against another WTO member's policies in case of its alleged breach of WTO rules. The process resembles a regular court procedure, whereby it is states that play the role of plaintiffs and defendants. The process usually involves consultations among the affected governments as well as an investigation by the appointed experts. Once a ruling is reached, and upheld by the Appellate Body in case of an appeal, it has a binding character, and its implementation is monitored by the WTO Dispute Settlement Body.[2] In addition, the WTO Secretariat undertakes periodic reviews of countries' trade policies and countries are required to notify certain measures covered by the relevant WTO agreements that can be discussed in the relevant WTO committees.

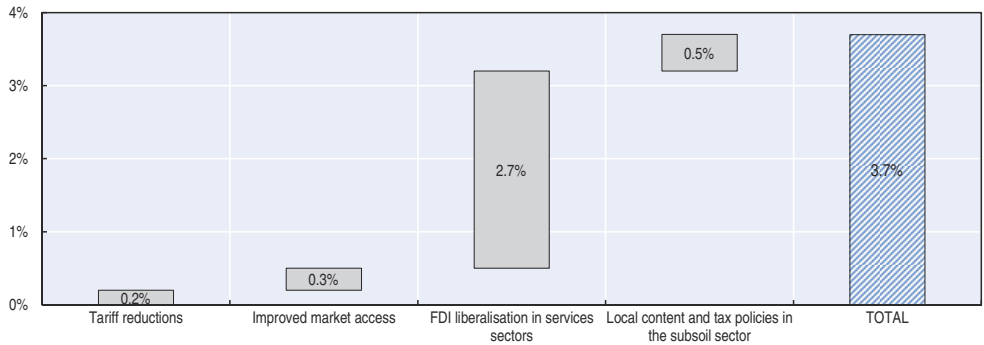
There are currently 22 countries undergoing the accession process, among whom Azerbaijan, Belarus and Uzbekistan. Russia joined the WTO in 2012, following a similarly long negotiation process as Kazakhstan.

Source: WTO (2015a), WTO (2015b), WTO (2015c).

Further opening to international trade and investment: Kazakhstan's WTO entry

Cumulatively, WTO entry was estimated to increase Kazakhstan's GDP by 3.7% in the medium- and 9.7% in the long run (with heterogeneity across economic sectors).[76] The opening of services sectors to FDI was predicted to have by far the largest impact on the Kazakh economy (over two thirds of total gains) (Figure 6.1). It is discussed first. While the impact of the tariff reform is predicted to be small, the positive effect of common WTO rules on the stability and predictability of Kazakhstan's tariff regime can be important (i.e. tariff bindings, customs valuation rules, etc.), and is discussed in this section as well.

Figure 6.1. **Estimated impact of WTO reforms on Kazakhstan's GDP (in the medium run)**



Source: Authors elaboration based on calculations in Jensen and Tarr (2007).

StatLink http://dx.doi.org/10.1787/888933452949

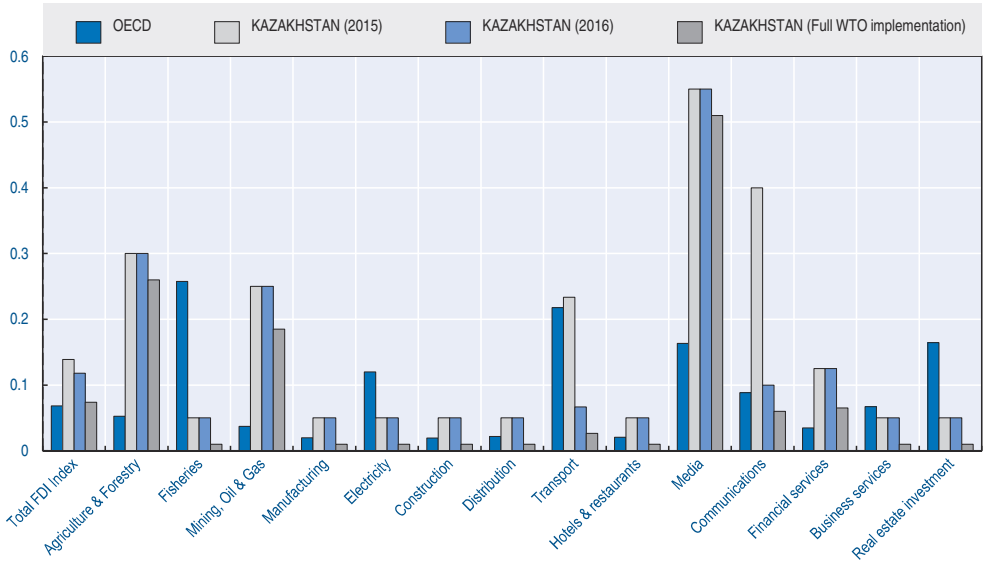
In some other areas, further reforms, going far beyond the country's WTO current commitments, will be required to help meaningfully reduce trade costs faced by firms. This applies, among others to trade facilitation and other reforms that aim to reduce at-the-border and behind-the-border barriers to trade, be it through changes to domestic regulatory process and closer co-operation with trading partners. Finally, investment in physical infrastructure for trade (i.e. road, railroads, etc.), including through greater participation of private sector infrastructure, will also play an important role.

Reforms in services sectors and other reforms with impact on investment

As mentioned above, pre-accession studies predicted that, among all the WTO-related reforms, the opening of services sectors would have the largest impact on country's economic welfare (accounting for two thirds of total gains or 2.7% of GDP in the medium run, see Figure 6.1). Kazakhstan has indeed made specific commitments in ten services sectors, including 116 sub-sectors, in its Schedule of Commitments under the WTO General Agreement on Trade in Services (GATS) (WTO, 2016c). The country also implemented a number of reforms liberalising its FDI regime throughout the 19 year-long time WTO accession period during which the terms and conditions of its entry were negotiated. Therefore, many reforms had been undertaken before the country acceded to WTO as well as in 2015 and early 2016 in order to ensure full compliance with the terms of its entry.

Figure 6.2 illustrates the impact of WTO reforms on Kazakhstan's FDI regime, in 2016 and 2020, by calculating the likely effect of the implementation of WTO commitments on the country's score on the *OECD FDI Regulatory Restrictiveness Index*. As can be seen, WTO commitments will help remove restrictions to FDI in

Figure 6.2. **FDI Regulatory Restrictiveness Index in Kazakhstan by sector after the WTO entry, 2015, 2016 and 2020**



Source: Authors' elaboration based on WTO (2015a; 2015c and 2015c) and the *OECD FDI Restrictiveness Index*.

StatLink http://dx.doi.org/10.1787/888933452950

some sectors Kazakhstan. For example, in telecommunications, the country committed to removing the maximum foreign equity limit in fixed-line telecommunications (of 49%), which had previously contributed to the Kazakhstan's elevated score on the FDI Index (Figure 6.2), within 2.5 years from its accession. Similarly, in the case of financial services, the commitment to allow branches of foreign-owned banks by 2020 will have a further liberalising effect.

Kazakhstan has also made horizontal commitments that will impact the degree of its openness in all services sectors. (See Table 6.1 below and Annex 6.A1 for a summary of the country's WTO commitments in this area.) This applies, among others, to the country's commitments relating to its local content policies (in mining and more broadly) and rules on hiring of foreign staff. For example, the requirement of local content in goods applied in the subsurface sector was removed altogether, and the share of foreign executives, managers and specialists that can be hired as intra-corporate transferees by firms is not subject to the national foreign labour quota (see Table 6.1). In addition, by 2020, the economic needs test (ENT) will no longer apply to foreign managers and specialists hired as intra-corporate transferees. As a result of these changes, the average FDI Index score of Kazakhstan would fall from 0.139 in 2015 to 0.074 (i.e. around the OECD average) by 2020 (Figure 6.2). Still, the commitments relating to local content and hiring of foreign staff are subject to

Table 6.1. **Kazakhstan's WTO commitments in services sectors**

Policy aspect	WTO commitment	Timeline	Changes already implemented
		Horizontal commitments	
Foreign personnel	Changes related to entry and temporary stay of business visitors and intra-corporate transferees (ICT), e.g. annual quota on foreign staff does not apply to ICTs (instead total number of foreign managers and specialists hired as ICTs cannot exceed 50% and no restrictions apply on executives); business visitors can enter visa-free for the period of 90 days; entry of foreign staff as ICT shall be permitted for 3 years, subject to certain conditions, and with a possibility of renewal.	By WTO entry: national quotas on foreign labour shall not apply to ICTs. By 2020: An economic needs test (ENT) shall not apply for hiring ICTs as managers and specialists after a five-year transition period.	Law 482-V "On Employment of 6 April 2016 and Government Resolution No. 45 of 13 January 2012, last amended on 31 March 2016
Government procurement	Request the status of an "observer" in the WTO Agreement on Government Procurement (GPA) and start of GPA membership negotiations	Start GPA accession negotiations (by tabling an Appendix 1 offer) within four years from WTO entry	None
Local content	Compliance of all laws, regulations and other measures within the scope of the TRIMS with the TRIMS Agreement and other WTO provisions. In subsurface and automotive sectors transition periods apply;[6] as do in the case of preferences granted under the free warehouse regime and special economic zones, SEZs[7] (see next column) With respect to local content in government procurement, rules will apply once the country joins the GPA- see above. In case procurement of services by investors in Subsurface, additional commitments apply,[8] including max. local content in services and applicable tender procedures	Compliance with WTO rules – by the time of WTO entry, except for: • contracts in the Subsurface sector (1 January 2021) • contracts in the automotive sector (1 July 2018) • preferences granted under the free warehouse regime and SEZs (1 January 2017) In addition, upon WTO entry, investors in Subsurface cannot be required to procure more than 50% of services from juridical persons of Kazakhstan. Also, when awarding subcontracts through a tender process, an investor shall, for period of six years, consider a putative 20% reduction in price to any bid submitted by a juridical person of Kazakhstan where at least 75% of subcontractors' qualified employees are citizens of Kazakhstan (50% after six years).	In the Subsurface sector, all local content requirements in goods have been removed and those in services and works cannot exceed 50% (Law No. 365-V of 27 October 2015)
Access to land	No commitment on foreign ownership of land for farming, agricultural production or forestry purposes. Bound at "none" for land used for construction sites or already under industrial or other buildings.	At the time of WTO entry	No change (The planned amendments to the Land Code, extending the maximum land rental period for foreigners, have been revoked in light of public protests.)

Table 6.1. **Kazakhstan's WTO commitments in services sectors** *(cont.)*

Policy aspect	WTO commitment	Timeline	Changes already implemented
	Sector-specific commitments		
Telecommunications	Foreign equity limit to be eliminated 2.5 years after the WTO accession (except for JSC "Kazakhtelecom"). Kazakhstan agreed to apply the WTO Basic Telecommunications Agreement	By mid-2018	Restriction already lifted: as of 1 January 2016, the max. foreign equity limit in fixed-line telecoms has been removed, and replaced by a screening and approval mechanism instead (i.e. in order to directly or indirectly own, use, dispose of or manage an aggregate of more than 49% of the voting shares in a legal entity in the sector, foreign investors must obtain a special government approval). Article 23, Law on National Security (N°527-IV), 6 January 2012, as amended.
Transport	Limited commitments (mostly unbound and with exceptions for an incorporation requirement whenever bound)	N/a	As of 1 January 2016 the 49% maximum foreign equity limit in air transport has been lifted (even though no WTO commitment exists). However, at the time of drafting, the government has been working on a draft law reinstituting the limitation. Given that there is no WTO commitment, the limit can be reinstituted.
Financial services	Foreign banks will be allowed to establish branches 5 years after accession. Foreign insurance companies will be allowed to establish branches 5 years after accession.	By 2020	Restrictions lifted as of 2020: Law No. 422-V[9] of 24 November 2015 already stipulates that, starting from 16 December 2020, non-resident banks, (re)insurance organisations, and companies, providing brokerage services will be allowed to open a branch, subject to terms and conditions established by national legislation.
Tourism	Cross-border travel agency and tour operator services to be allowed 2 years after accession	By 2017	None

* In case of investment contracts signed prior to 1 January 2015, all WTO-inconsistent measures in the Subsurface and automotive sector need to be phased out by 1 January 2021 and 1 July 2018, respectively, or by the time of the expiry of the contact (whichever comes sooner). For contracts signed after 1 January 2015, no TRIMs-inconsistent measures can be included or maintained upon the country's WTO accession.

Source: Authors' elaboration based on WTO (2015a; 2015b; 2015c) and information provided by the Government of Kazakhstan.

several transition periods and exceptions (Table 6.1), which means that firms may not immediately perceive the results. For example, exceptions exist in case of local content requirements applied in the subsurface sector (up to 2021), the

automotive sector (up to 2018) and in special economic zones (SEZs) (up to 2017), and purchases by state-owned firms.[3] In the area of hiring foreign staff, also several conditions and phase-out periods apply.[4] In addition, as also noted in Chapter 2, the government will need to ensure that the administrative procedures in this area do not serve as a *de facto* barrier to hiring foreign personnel, impeding firms' ability to hire talent and compete. As discussed in the next section, the country has made some commitments relating to regulatory transparency in services sectors in which it made specific GATS commitments to ensure that licensing requirements and other administrative procedures do not pose a barrier to entry were FDI restrictions were removed.

Finally, in several relatively closed sectors Kazakhstan has made little or no commitments. For example, in the case of air transport, one of the most protected sectors in Kazakhstan as measured by the FDI Index, no commitment regarding the lifting of the maximum foreign equity limit was made.[5] While the government still unilaterally lifted the limit in early 2016, it is free to reinstate the limit in the future, given the lack of the WTO commitment; and the plans to do so appear to already exist (see Chapter 2). Such uncertainty is likely to *de facto* deter any investments above the 49% threshold. Last but not least, no commitments have been undertaken in regards to the maximum rental time of land for agricultural and forestry purposes by foreigners (currently of 10 years). As can be seen in Figure 6.2, the restriction contributes to the country's relatively high score on the FDI Index. The maximum rental time of such land by foreigners in Kazakhstan is much shorter than in OECD countries, and may be holding down Kazakhstan's potential in agricultural production (OECD, 2013). Given high sensitivity of reforms in this area, illustrated by recent protests (see Chapter 7), further liberalisation appears difficult in the short term, and would require the government to engage in further communication and dialogue with the population on the reform's likely consequences – both real and perceived.

In summary, while changes to horizontal or sector-specific restrictions to FDI required by the WTO entry have helped significantly liberalise Kazakhstan's FDI regime over time, in some sensitive areas, identified as restrictive or burdensome in the past (OECD, 2012), the impact will be felt only gradually and the removal of de jure restrictions on FDI will need to be accompanied by further investment facilitation reforms to ensure improved market access in practice.

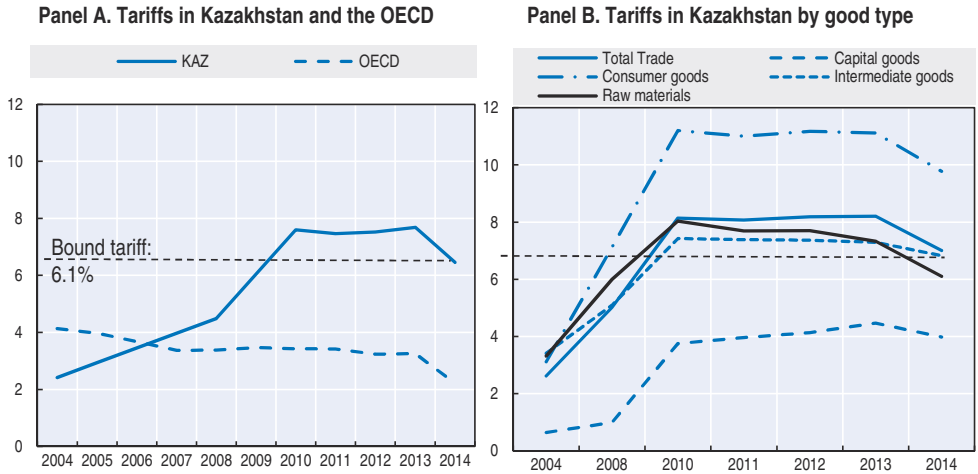
Tariffary and quantitative restrictions on trade

Even though tariff reductions were estimated to account for only 6% of the estimated gains from Kazakhstan's WTO entry, the commitments in this area can have important implications on the stability and predictability of the country's trading environment that are difficult to capture in standard trade

models. For example, tariff bindings can help prevent future tariff increases above the agreed upon levels and the common WTO rules on customs valuation and tariff classification reduce the variation in tariff application in practice. These aspects are described in more detail below.

The WTO tariff binding means that a country cannot apply tariffs above the level agreed as part of its Goods Schedule with other WTO members (see Box 6.1). Following the WTO accession, Kazakhstan's overall level of import tariffs has been bound at, and cannot exceed, 6.1%.[10] This implies a tariff reduction from the current tariff level and can help provide an additional stabilising mechanism to Kazakhstan's tariff system, which was subject to important tariff increases over the past couple of years (Figure 6.3) as a result of the country's integration into the Eurasian Customs Union (ECU), and later the Eurasian Economic Union (see Box 6.2). While in the early 2000s the average applied import tariff level in Kazakhstan was 2%, below the OECD average at the time (of 4%), it increased three times following the entry into force of the ECU and adoption of the common external tariff (CET) in 2010.[11] One simulation (World Bank, 2015a) foresees that, upon full implementation of WTO reforms by 2020, Kazakhstan's import tariff levels would have largely returned, on trade-weighted basis, to its pre-ECU period and tariff dispersion would have reduced as well. The authorities are currently negotiating with other ECU members an administrative mechanism that will allow Kazakhstan to implement such tariff reductions without imposing additional tariff reductions onto the other ECU members, but its administrative implementation may nevertheless impose transaction costs at the border on certain investors and traders.

Figure 6.3. **Applied import tariffs in Kazakhstan and OECD countries (in %), 2004-14**



Note: Simple average is shown. Tariff data for Kazakhstan for years 2005, 2006, 2007, and 2009 is not available.
Source: Authors' calculations using UN TRANS database.

StatLink http://dx.doi.org/10.1787/888933452966

Box 6.2. **The Eurasian Customs Union and the process of Kazakhstan's integration**

The Eurasian Economic Union (EAEU) is an economic union comprised (as of December 2015) of Kazakhstan, the Russian Federation, Belarus, Kyrgyzstan and Armenia. A treaty aiming for the establishment of the EAEU was signed on 29 May 2014 by the leaders of Belarus, Kazakhstan and Russia, and came into force on 1 January 2015. Armenia's and Kyrgyzstan's EAEU Accession Treaties were signed on 9 October and 23 December 2014 and came into force on 2 January 2015 and 6 August 2015, respectively. The creation of the EAEU marks a stage in the economic integration process between the concerned countries, and was preceded by the Eurasian Economic Community (EurAsEC), whose goal was to strengthen economic integration between the countries in the Eurasia region that belong to the Commonwealth of Independent States.[12]

Kazakhstan together with five other EAEU members is also part of the Eurasian Customs Union (ECU).[13] It was formed in 2010 by three founding members – Belarus, Kazakhstan and Russia, and subsequently acceded by Armenia (2 January 2015) and Kyrgyzstan (6 August 2015). All ECU members share a common external tariff and agreed to a common legal and institutional framework governing the Union, including a mechanism for distributing the customs duties collected at the common border, abolition of customs controls within the ECU territory and a common regulatory and decision making body – i.e. Customs Union Commission replaced by the Eurasian Economic Commission on 2 February 2012.[14]

The Eurasian Economic Commission (EEC) is a permanent regulatory body of the Eurasian Economic Union. It is responsible for setting of new laws and regulations in certain areas under its competence (including in relation to the CET and other trade related procedures), implementing decisions taken at the EAEU level, upholding the EAEU treaties and managing the day-to-day business of the EAEU.

For further information, see the EEC website: *www.eurasiancommission.org/en/Pages/about.aspx*.

Besides the stabilising effect of tariff binding on the country's tariff regime, common WTO rules on customs valuation[15] can also help reduce the variation in tariff application in practice.[16] This is because Kazakhstan's Customs Code (under review at the time of writing), the ECU Customs Code, and the ECU Agreement on Customs Valuation are now subject to relevant WTO rules on customs valuation, limiting the risk of arbitrary treatment at the border and imposition of higher import values than suggested by the actual value of goods being shipped. The implementation of additional trade facilitation provisions enshrined in the WTO Trade Facilitation Agreement,

such as a more extensive use of advanced rulings, could also help improve the practicability of customs processes in practice (see next section).

Last but not least, the WTO rules on quantitative trade restrictions can also have a stabilising effect on Kazakhstan's trading environment. Prior to the WTO entry, Kazakhstan regularly took recourse to quantitative restrictions on exports in the agricultural sectors. Namely, it frequently introduced bans on exports of certain grains and other agricultural products (see Table 6.2 below and OECD, 2013) in an attempt to control domestic prices. At times, these measures introduced additional uncertainty into the market and reduced local firms' export opportunities (OECD, 2013). Export bans and quantitative restrictions on commercial products are prohibited under WTO rules, except in certain circumstances justified under existing WTO provisions.[17] Should these rules and potential challenges under the WTO Dispute Settlement Mechanism dissuade Kazakhstan from use of such measures, it could reduce the noise in market signals and have a stabilising effect on investment opportunities of firms operating in the sector.[18]

Table 6.2. **Temporary export bans of agro-food products imposed by Kazakhstan, 2007-12**

Date	HS Code	Document
23.10.2007-01.02.2008	1206 00 (sunflower seeds) 1512 (sunflower oil)	Government Resolution No. 976 of 20.10.2007
1.04.2008-01.10.2008	1206 00 (sunflower seeds) 1512 (sunflower oil)	Government Resolution No. 260 of 18.03.2008
13.09.2008-01.04.2009	1205 (rapeseeds) 1507 (soya oil) 1514 (rapeseed oil)	Government Resolution No. 777 of 28.08.2008
01.10.2008-01.04.2009	1206 00 (sunflower seeds)	Government Resolution No. 930 of 08.10.2008
27.10.2008-01.04.2009	1201 00 (soybeans) 1207 20 (cotton seeds) 1207 99 (other oilseeds)	Government Resolution No. 930 of 08.10.2008
20.10.2010-20.04.2011	1008 10 (buckwheat) 1103 19 (buckwheat cereal preparations) 1201 00 (soybeans) 1206 00 (sunflower seeds) 1207 99 (cotton seeds) 1507, 1512, 1514, 1515 11, 1515 19 (vegetable oils), vegetable and animal fats (1516)	Government Resolution No. 1024 of 05.10.2010
01.09.2010-01.03.2011	1701 99 (white sugar)	Decision of the Customs Union Commission No. 334 of 16.04.2010
11.05.2010-01.07.2010	1701 99 100 (white sugar), 1701 99 900 (other sugar)	Decision of the Customs Union Commission No. 334 of 16.04.2010
29.10.2011-29.02.2012	1512 1 (sunflower oil, safflower oil, cotton oil)	Government Resolution No. 942 of 23.08.2011

Source: OECD (2013) based on information from the Eurasian Economic Commission.

The simultaneous effect of being bound by different rules on tariff, quantitative restrictions and other measures with impact on trade can help the government ensure greater coherence in the area of trade policy. Being subject to WTO rules on export restrictions, subsides, and other rules, means that such actions should be less frequent in the future, and may allow for an emergence of clearer market signals in the agricultural and other sectors.

Trade facilitation

WTO entry also means being subject to the growing disciplines on trade facilitation and rules on certain border procedures, notably as enshrined in the WTO Trade Facilitation Agreement (TFA). Being a landlocked country, improving the efficiency of border procedures as well as trade infrastructure should be a priority for Kazakhstan to attempt to compensate for some for the geographical disadvantages. Meanwhile, Kazakhstan is scoring poorly on efficiency of its border procedures. For example, Kazakhstan ranked 119th out of 190 economies in the area of ease of trading across borders on the World Bank's *Doing Business* indicators in 2017, which is significantly below the average score and has remained unchanged for several years. This appears to be consistent with the insights from the available firm-level data: it takes longer for an average firm to clear exports and imports through customs in Kazakhstan than elsewhere in the region; and only 5% of firms do export, as compared to 19% in the region as a whole (Figure 6.4).

Figure 6.4. **Firms' trade experience in Kazakhstan compared to other countries, 2013**

In %

* This indicator is computed using data from manufacturing firms only.

Source: Word Bank's *Enterprise Survey*, 2013.

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The World Bank (2015a) estimated that, if reforms associated with Kazakhstan's WTO entry were to be accompanied by a 30% decrease in the costs

of trade facilitation, the overall impact on welfare would increase by about one percentage point of GDP per year (which implies a nearly 5% GDP gain by 2020). The OECD analysis using the OECD Trade Facilitation Indicators (TFI) also suggests that implementation of a comprehensive trade facilitation reform, involving improvements across all eleven areas covered by the TFA, could reduce trade costs by about 13% in upper middle-income countries like Kazakhstan (Box 6.3). While these estimates likely represent the upper bound of

Box 6.3. **What are the OECD Trade Facilitation Indicators and how does Kazakhstan perform?**

As goods cross borders many times, first as inputs and then as final products, fast and efficient customs and port procedures are essential. Unduly complex processes and documentation raise costs and cause delays, with businesses and consumers ultimately bearing the cost. Conversely, countries where inputs can be imported and products and services exported within short and reliable timeframes are more attractive investment locations.

To help governments improve their border procedures, reduce trade costs, boost trade flows and reap greater benefits from international trade, OECD has developed a set of Trade Facilitation Indicators (TFIs) that identify areas for action and enable the potential impact of reforms to be assessed. The OECD indicators cover the full spectrum of border procedures for more than 160 countries across all income levels, geographical regions and development stages. The indicators seek to reflect not only the regulatory framework in the concerned countries, but delve, to the extent possible, into the state of implementation of various trade facilitation measures. The TFIs track the policy areas of the WTO Trade Facilitation Agreement (TFA), namely:

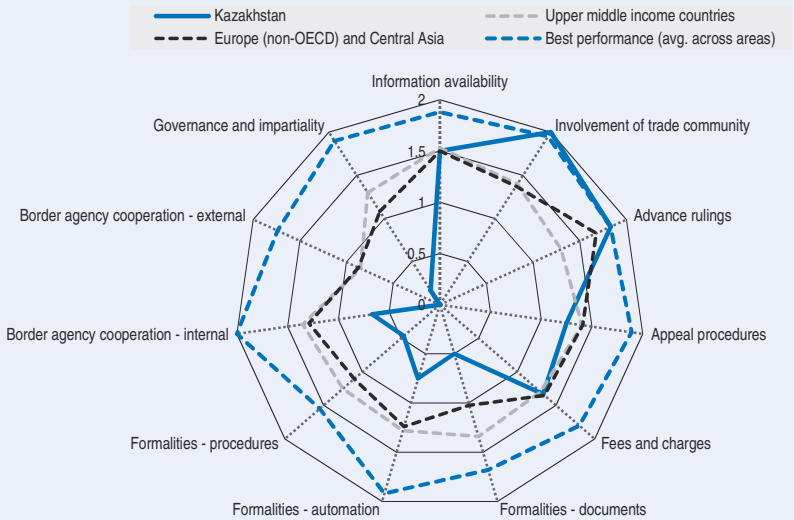
- Information availability;
- Involvement of the trade community;
- Advance rulings;
- Appeal procedures;
- Fees and charges;
- Formalities (Documents, Automation, Procedures);
- Border agency co-operation (Internal and External);
- Governance and impartiality.

Estimates based on the indicators provide a basis for governments to prioritise trade facilitation reforms and to mobilise technical assistance and capacity-building efforts in a more targeted way. Such analysis shows that the potential trade costs reduction from implementation of all the options contained in the TFA range between 10.4% and 17.4% for all countries, and about 13% for upper middle-income countries like Kazakhstan. Streamlining

Box 6.3. **What are the OECD Trade Facilitation Indicators and how does Kazakhstan perform?**

and automating border processes, the use of risk assessment as well as the use of advance rulings are estimated to have the largest impact on reducing trade costs of such countries (Moïsé and Sorescu, 2013; OECD, 2014). Given that Kazakhstan lags behind its income group in the area of formalities (see figure below), further progress in streamlining and automating border procedures could have a sizable impact.

Kazakhstan's performance on the OECD Trade Facilitation Indicators, 2016



Source: www.oecd.org/trade/facilitation/indicators.htm.

possible gains, government could consider undertaking key reforms to reap benefits. For example, streamlining and automating border processes, including through the use of risk management processes – where Kazakhstan lags most behind the average – are found to have the most impact on trade costs in countries like Kazakhstan. This area should hence be prioritised by the government, as already envisaged in the President's 100 administrative steps and other strategic documents.[19]

Further reform in this area could include implementing the Single Window for Trade,[20] operationalising the Authorised Economic Operators programme,[21] introducing the electronic customs clearance and payment systems[22] as well as improving the border risk management system and intra-agency co-operation

in Kazakhstan.[23] To support such trade facilitation reforms, the authorities are in the process of implementing several modernisation programmes.[24] They also undertook a diagnosis of the country's readiness to implement the WTO TFA provisions.[25]

While these efforts are laudable, given that several of the on-going reforms have been planned for years,[26] better monitoring of progress as well as an allocation of adequate resources and targeted capacity-building programmes will be crucial to help the government achieve the intended results. One tool to facilitate monitoring is a conduct of a Time Release Study (TRS), which has been used in numerous OECD and other economies to trace average time spent by goods at each stage of the border process, help identify bottlenecks, and monitor reform implementation (Box 6.4). The experience of other countries

Box 6.4. **Time Release Study: A trade facilitation benchmarking tool**

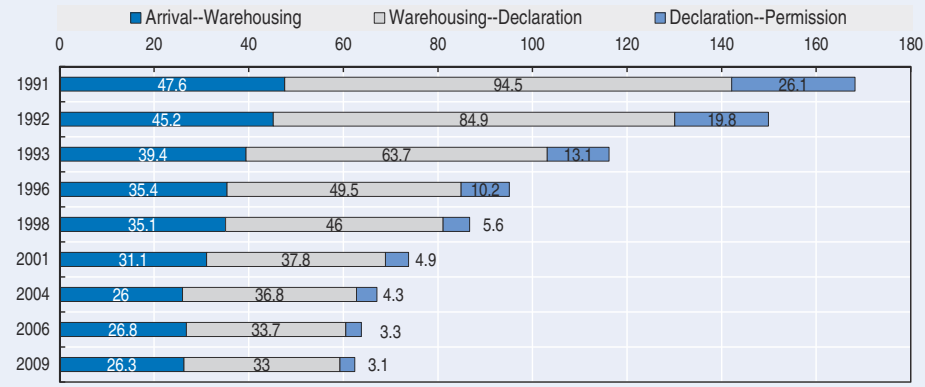
A Time Release Study (TRS) is a standardised method to assess the trade facilitation performance of Customs administrations and other agencies and private entities operating at the border (e.g. brokers, forwarding and shipping agents, carrier.) It was elaborated following similar initiatives undertaken by the Customs Administrations of Japan and the United States and endorsed by the WCO in 1994, then shaped into a methodological Guide in 2002. TRSs serve the principles of the WCO Kyoto Convention to simplify and harmonise customs procedures internationally to reduce overall trade transactions costs. A TRS involves a detailed diagnostic of the efficiency of border processes and identifies potential corrective actions. As such, it is a powerful performance assessment tool for customs and other border services and provides a pre-reform benchmark that can serve a number of policy purposes:

- When undertaken over a series of years, it allows monitoring the evolution of progress and assessment of the efficiency of particular reform measures. For example, Japan's successive TRS exercises (there were 9 between 1991 and 2010) helped sustain reforms that reduced sea cargo intervals from 7 days in 1991 to 2.6 days in 2009 whereby customs clearance takes on average 3.1 hours (see the figure below). Japan customs also use TRS to measure impact of particular reforms such the implementation of the Authorised Economic Operator (AEO) status. In 2009, AEOs in Japan experienced average times between goods arrive and release over a day shorter than non-AEOs.
- Today a number of countries use TRS as a tool for internal benchmarking and to support strategic planning, including the United States, Japan, Mexico, Korea, Australia, Colombia and others. For example, the Australian Customs and Border Protection Service conducted a Time Release Study (TRS) in 2007, published the results in 2009, and decided to conduct the study on an annual basis as an aid to strategic planning. The TRS has covered all border-related procedures, including Sanitary and Phytosanitary (SPS) procedures managed by 41 other concerned government agencies, and identified 1.3 days of interval between the arrival and release for sea cargo.

Box 6.4. **Time Release Study: A trade facilitation benchmarking tool** *(cont.)*

- Most recently, countries have also started using TRS in an international and regional context. One example is the Trans-Tasman TRS carried out in 2010 as a joint effort by the Australian and New Zealand Customs Services in order to identify opportunities for streamlining trade between the two countries. Customs officers in both services worked together on the scope of the TRS, and the study lead to revision of 4 border procedures responsible for delays. Another example is a pilot TRS carried out in a northern corridor of the East African Community (EAC) which aimed to identify bottlenecks in the flow of cargoes from/to Mombasa sea port in Kenya to/from customs office in Kampala, Uganda.

Monitoring of trade facilitation reforms using TRS in Japan, 1991-2009



Source: Japanese Customs.

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Overall, a TRS represents a powerful performance assessment tool for customs and other border processes, which can help monitor progress over time, aid strategic planning, and facilitate reform in an international context. As such it can support countries efforts to increase their integration into GVCs, and on a global level to support the overall goal to harmonize customs procedures and reduce trade transaction costs.

Source: OECD, *Matsuda* (2012).

shows that TRS can be a powerful tool to identify specific lacuna in the entire body of border processes (not only customs procedures), facilitate inter-governmental coordination, and support strategic planning and oversight of on-going reforms. The government could undertake such a study in collaboration with the World Customs Organisation and consider making its results publically available to help raise awareness about the progress made and remaining challenges as well as help generate support for reforms.

In the long run, a substantial improvement in the time and reliability of border procedures coupled with increased investment and realisation of infrastructure projects can help significantly reduce the cost of trading in Kazakhstan. While the WTO accession, including the ratification of the WTO TFA by Kazakhstan, will assist the government in the process, further domestic reform, including effective implementation and monitoring of progress will be crucial to help tangibly reduce the costs of trading in Kazakhstan.

Other regulatory barriers to trade and transparency

Beyond improvements in trade facilitation, a progressive removal of other non-tariff barriers (NTB) to trade (such as overly burdensome technical regulations or opaque licensing requirements), and improving the overall quality and predictability of the regulatory environment for trade activity, will be critical to help increase trade opportunities for Kazakh firms and making Kazakhstan a more attractive investment destination. For example, a recent survey by UNECE (2014) shows that, on average, NTBs affect 30% of importers and exporters in Kazakhstan, and in some sectors they significantly prolong the time it takes to import and export.[27] As Kazakhstan has the ambition of diversifying its trade structure away from oil products towards goods and services that may face higher regulatory requirements (such as agro-food or manufactured products), engaging in negotiations with its main trading partners–at the EAEU level but also beyond–about progressive reduction or NTBs will be an important aspect of reducing trade costs faced by firms.

It appears that EAEU-level regulations are the main source of NTBs in Kazakhstan.[28] Proving compliance with technical regulations, including sanitary and phyto-sanitary (SPS) and conformity assessment, prove most burdensome. Kazakhstan is hence facing a double challenge of using EAEU integration to reduce the regulatory barriers to trade stemming from other EAEU members' legislation, while avoiding establishing new barriers, at the EAEU level, which could render trade with third countries more difficult (i.e. cause trade diversion).[29] The government is conscious of this challenge, and recognises that further progress in this area will require changes to the domestic and EAEU-level regulatory processes, progressive adoption of international standards, improvements in the accreditation and certification infrastructure as well as further coordination with the other trading partners through further international trade agreements and regulatory co-operation (discussed next).

WTO accession does involve certain transparency-enhancing measures and measures relating to technical barriers to trade (TBT) that will be binding to Kazakhstan upon its entry. For example, several WTO provisions require Members to publish laws, decrees, resolutions or other measures of general application pertaining to or affecting trade in goods, services or intellectual

property rights before they can be enforced.[30] Kazakhstan also committed to publish all laws, regulations, decrees, decisions and administrative rulings, whether issued or adopted by the Republic of Kazakhstan or by a competent body of the EAEU; and to providing a reasonable time to WTO members and other interested parties to comment (normally not less than 30 calendar days) before the measure is adopted.[31] The Protocol also stipulates that Kazakhstan will comply with notification requirements embedded in various WTO Agreements,[32] provide the right for an independent review of its conformity with WTO obligations;[33] and undergo periodic reviews of its trade policy by the WTO Secretariat.

In addition, as mentioned earlier, Kazakhstan made several broad commitments relating to governance of the country's services sectors in its WTO Accession Protocol. For example, it committed to ensuring that licensing procedures would not in themselves constitute a restriction on the supply of service in the services sectors in which it made specific WTO commitments.[34] It also agreed to abide to a set of specific guidelines relating to the process of setting and implementing licensing requirements and procedures in these sectors (e.g. regarding their publication, review and approval process, and notification about the final decision).[35] The government also committed to ensuring that relevant regulatory authorities in these sectors would not be accountable to any service suppliers they regulated; and that, where practicable, regulations of general application in these services sectors shall be published in advance; an opportunity to comment regulatory proposals shall be provided to interested parties, and a reasonable time between the publication of a proposed regulation and its entry into force shall be ensured.[36] If the opportunity of existence of these specific commitment is seized by the Government to improve the regulatory transparency and quality in these sectors, it could translate into a more pro-competitive and transparent regulatory environment in these sectors, making them more attractive for investment.

All these measures help monitor the changes in Government's actions in the area of trade policy and, hence, can help increase their transparency. They are subject to the WTO dispute settlement mechanism and have been employed in disputes more frequently over time, which may increase compliance.[37] Other WTO members are also bound by the same WTO rules in this area, and Kazakhstan can monitor and require notifications or explanations from other WTO members as well. Still, such obligations remain relatively broad, and rarely supplant the need for, on the one hand, continued domestic reform to improve the quality of domestic regulations and remove unnecessary administrative burdens to trade and, on the other, further co-operation and commercial agreements with trading partners to help reduce the incidence of TBTs abroad.

Further trade integration – going beyond WTO

As highlighted above, WTO accession marks an important step in Kazakhstan's economic integration with the rest of the world. Still, trade costs faced by Kazakh firms, including foreign investors in investing in the country, can be reduced further through signing of further preferential trade agreements, as well as development of physical infrastructure for trade.

Up until now, Kazakhstan has mainly signed Free Trade Agreements (FTAs) with other CIS countries, as well as Georgia and Serbia (Table 6.3), and has continued its integration within the Eurasian Economic Community. Most recently, the Treaty on Eurasian Economic Union (EAEU) was signed on 29 May 2015, and came into effect on 1 January 2015, creating an economic union between Kazakhstan, Russia, and Belarus that provides for free movement of goods, services, capital and labour as well as allowing for progressive

Table 6.3. **List of preferential trade agreements signed by Kazakhstan**

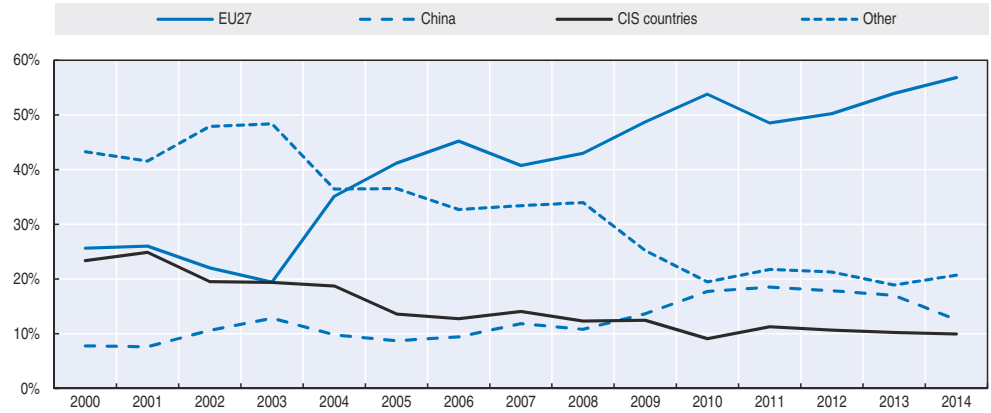
No.	Title of agreement	Parties	Status	Date of signature	Date of entry into force
1	Kazakhstan-EU Agreement on Enhanced Partnership and Co-operation (EPCA)	EU; Kazakhstan	Signed	21-12-2015	01-05-2016
2	Eurasian Economic Union - Viet Nam FTA	Eurasian Economic Union; Viet Nam	Signed	29-05-2015	
3	Treaty on Eurasian Economic Union (EAEU)	Eurasian Economic Union	In force	29-05-2014	01-01-2015
4	Belarus-Kazakhstan-Russia Agreement on Services and Investment	Belarus; Kazakhstan; Russian Federation;	In force	09-12-2010	01-01-2012
5	Common Economic Zone Agreement (2003)	Belarus; Kazakhstan; Russian Federation; Ukraine	In force	19-09-2003	20-05-2004
6	EC-Kazakhstan Co-operation Agreement	EU; Kazakhstan	In force	23-01-1995	01-07-1999
7	Armenia - Kazakhstan FTA	Armenia; Kazakhstan	In force	02-09-1999	25-12-2001
8	Eurasian Economic Community (EAEC)	Belarus; Kazakhstan; Kyrgyz Republic; Russian Federation; Tajikistan	In force	29-03-1996	08-10-1997
9	Georgia - Kazakhstan FTA	Georgia; Kazakhstan	In force	11-11-1997	16-07-1999
10	Kazakhstan- Kyrgyz Republic FTA	Kazakhstan; Kyrgyz Republic	In force	22-06-1995	11-11-1995
11	Kazakhstan - Ukraine FTA	Kazakhstan; Ukraine	In force	17-09-1994	19-10-1998
12	Treaty on a FTA between members of the Commonwealth of Independent States (CIS)	Armenia; Belarus; Kazakhstan; Kyrgyz Republic; Moldova, Republic of; Russian Federation; Tajikistan; Ukraine	In force	18-10-2011	08-12-2012
13	Kazakhstan - Serbia FTA	Kazakhstan; Serbia	In force	07-10-2010	10-01-2012
14	Agreement on the Customs Union between the Russian Federation, Belarus and Kazakhstan	Belarus; Kazakhstan; Russian Federation	In force	20-01-1995	03-12-1997

Note: For a full list of RTAs signed by Kazakhstan consult Annex 23 of the country's WTO Accession Protocol.
Source: OECD based on Kazakhstan's WTO Accession Protocol and the WTO Regional Trade Agreements Information System (RTA-IS) (*http://rtais.wto.org/UI/PublicMaintainRTAHome.aspx*).

harmonisation in relevant legislation and coordination of trade and economic policies. Studies estimate that the removal of NTBs among the member countries within that process as well as improved border coordination and joint trade facilitation reforms, described earlier, could bring important gains to Kazakhstan, outweighing the costs related to trade diversion.[38] The government should therefore pursue further diplomatic efforts to facilitate harmonisation, whenever possible avoiding the introduction of standards and regulations that are different or more stringent than international standards and could unduly impact its trade opportunities with other countries.

In parallel Kazakhstan has also been strengthening its relationship with the EU, which remains its main trading partner (Figure 6.5). The terms of Kazakhstan-EU relationship have been historically defined by the Partnership and Co-operation Agreements, the first one having been signed in 1995 and the most recent one, Enhanced Partnership and Co-operation Agreement (EPCA) on 21 December 2015.[39] The agreement covers a whole array of trade policy issues, including trade in goods and services, trade facilitation, intellectual property rights, TBTs and regulatory co-operation, competition, treatment of state-owned enterprises, and many others. It also includes a dedicated dispute settlement mechanism to which the provisions of the Agreement are subject, with certain exceptions.[40] In some cases, the agreement refers to and reaffirms WTO commitments (e.g. on import and export restrictions); in others it includes additional provisions (e.g. IPR protection, SOEs, TBTs and regulatory co-operation), and provides a basis for deepening the trade-related reform process. Kazakhstan could benefit from further co-operation and capacity building in these areas, and notably regulatory co-operation and border procedures mentioned above, to facilitate trade in non-traditional products. In

Figure 6.5. **Kazakhstan's exports by partner country, 2000-14**



Source: Authors' calculations using the UN COMTRADE database.

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addition, some of the tariff hikes on certain Kazakh products could be reduced to limit the disadvantage placed on some firms (Figure 6.A2.2. in the Annex).

Finally, given this binary approach to trade negotiations–oriented primarily towards the EU and the EAEU, Kazakhstan may have unexploited opportunities for closer economic integration with other countries, such as China or Iran, and other economies with whom it benefits from a relatively high trade complementarity (World Bank, 2015a). This could also help reduce Kazakhstan's dependence on the European and CIS markets. Given that tariffs faced by Kazakh exporters in some regions are still relatively high (Table 6.4), and these tend to be markets where NTMs for Kazakh products may be relatively low (given the less developed regulatory environment than in the EU market, for example), there could be scope for exploring further options for singing new FTAs and building on Kazakhstan's recent trade reform momentum.

Table 6.4. **Import tariffs applied on Kazakh exports by region, 2015**

Tariff type	Simple average	Weighted average
CIS countries	0.00	0.00
EU	3.89	0.58
OECD members	5.37	2.29
Middle East and North Africa*	7.69	5.98
East Asia and Pacific*	8.09	5.45
South Asian countries*	10.14	5.42
Latin America and Caribbean*	11.48	7.01

* Low and Middle income only.
Source: OECD calculations using the UN TRAINS database.

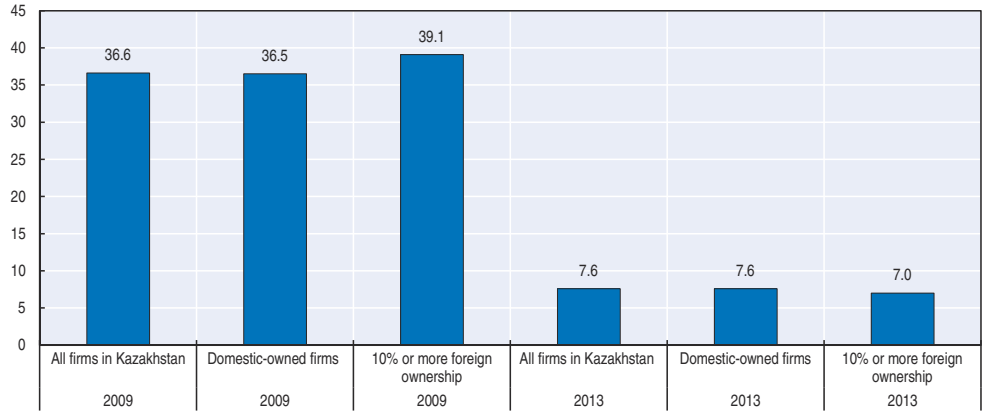
Encouraging more private investment into infrastructure

Trade facilitation and other trade reforms can do little to meaningfully reduce trade costs faced by firms and help them connect to global markets if the country's underlying infrastructure is undeveloped or of poor quality. This is particularly important in the case of landlocked countries, like Kazakhstan, that already pay a transport premium and relay on a well-developed network of surface transport corridors and transit routes to connect with the outside world.

Despite improvements, infrastructure in Kazakhstan requires further investments to help reduce costs and connect far-flank regions to markets, and benefit from its strategic location. According to one study, the share of transport cost to the total cost of goods in Kazakhstan is 8% in the case of railway transportation and 11% in case of road transport, compared to 4-4.5% in industrialized countries (Rana, 2016). The country also ranked 79th out of 140 countries on the quality of transport infrastructure in the World Economic Forum's *Global Competitiveness Index* 2015-2016, with the quality of roads being

particularly badly evaluated (107th rank). Still, some international organisations point to progress made in recent years. For example, the country improved its ranking on the World Bank's *Logistics Performance Index* (LPI) from 137th place in 2007 to 57th place in 2016. Likewise, according to the World Bank's *Enterprise Survey*, while 37% of firms identified transport as a major constraint to doing business in 2009, this share dropped to about 8% in 2013 (Figure 6.6). These results may indicate a certain degree of optimism among market participants about the on-going efforts. Going forward, improved regulatory framework for private sector participation in infrastructure – identified as a constraint in the previous review – and observance of due process in project selection and implementation will be critical to ensure planed future projects are duly implemented.

Figure 6.6. **Percent of firms identifying transportation as a major constraint, 2009 and 2013**



Source: World Bank Enterprise Survey.

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Improvements in the coverage and quality of infrastructure require investments – both public and private. Mobilising private investment in infrastructure can be a way to gather additional capital as well as to reap additional efficiency gains in project delivery or operations (OECD, 2015). As such, the *Policy Framework for Investment* recommends a list of questions for the government's consideration to allow for a creation of an enabling environment for investment in infrastructure (Box 6.5).

In the previous *Review*, the OECD noted that "given the importance of infrastructure for national and international integration in such a large and remote country as Kazakhstan, the stock of infrastructure is inadequate and outdated". It noted that the inadequacy of the legal framework for Private-Public Partnerships (PPP) as well as high presence of state-owned enterprises in several segments of the infrastructural markets are an important factor limiting private participation in infrastructure.

Box 6.5. **The enabling environment for investment in infrastructure**

The OECD *Policy Framework for Investment* (PFI) provides policy makers with a list of questions for consideration to help create an enabling environment for investment in infrastructure, which is provided below. They relate among other to the adequacy of the domestic legal framework, the appropriate regulatory environment as well as the existence of due processes in project selection and implementation to ensure transparency and reduce the risk of mismanagement and corruption.

- What is the overall policy and institutional framework for private investment in infrastructure and how has it been informed by international good practices?
- Does the government have a strategy for public-private partnerships, and if so are its provisions and institutions consistent with the broader regime for infrastructure procurement? Does the legal basis for PPPs avoid conflicts with other legislation, either through a PPP act or through sectoral legislation explicitly admitting PPP delivery modes?
- Is an open and non-discriminatory investment environment in place for infrastructure providers, including between foreign and domestic and new providers and incumbents? What are the restrictions on foreign investment in infrastructure sectors, if any? To what extent are foreign private companies able to compete on an equal basis with both domestic companies and foreign state-supported companies in seeking access to infrastructure markets?
- What modalities for private investment in infrastructure does the government promote? What are the most common concession/PPP modalities across sectors? Is the combined procurement of design, construction and long-term operation allowed? Is the bundling of small infrastructure projects possible in order to minimise transaction costs and thus facilitate attracting investors? Are concession contracts allowed to include no-compete (or exclusivity) clauses? Please describe the main characteristics of licences and concessions.
- How do regulatory agencies and the competition authority co-ordinate in assessing the costs and benefits of unbundling network industries and ensuring adequate competition in infrastructure markets?
- To what extent do regulatory and competition authorities have adequate political support and independence to denounce anti-competitive behaviour by infrastructure providers (including by SOEs), particularly when challenging vested interests?
- Are there clear and transparent guidelines to ensure predictability and consistency in selecting, preparing and procuring infrastructure projects? Are the institutional roles and responsibilities of agencies responsible for these different phases clearly identified in the legal framework? Are these

Box 6.5. **The enabling environment for investment in infrastructure** *(cont.)*

agencies adequately staffed in number and skills to allow the agency to work at the level required by the industry?

- Are there regulations to guarantee full disclosure of all project-relevant information between public authorities and their private partners, including on the state of pre-existing infrastructure?
- What forms of infrastructure procurement exist and subject to what conditions? When unsolicited proposals are permitted, are there distinct, clear and transparent selection procedures for such proposals? To what extent do existing procedures adequately address the specific transparency issues such proposals entail?
- Are there any preference margins for domestic versus foreign bidders, or for SMEs versus larger bidders, in infrastructure procurement procedures? If so, what is the extent of these margins and do they vary according to the sector and size of the project?
- What role does the government play in ensuring that corruption is not involved in the procurement process? What steps have been taken to minimise the risk of bid-rigging in infrastructure contracts?
- Are competition authorities involved in the procurement process, and how? How are the responsibilities co-ordinated between procurement agencies and the competition authority?
- Do selection procedure ensure appropriate due diligence of bidders to assess the realism of the bids, their financial soundness, risk profile and prior experience? Do procedures adequately address any potential conflict of interest?
- Are authorities legally required to set and publicise the criteria according to which infrastructure providers will be chosen when an invitation to tender is made? Are the performance standards required from winning bidders carefully defined and publicised in advance of tenders?
- Are authorities required publicly to explain award decisions in terms of careful and verifiable references to those criteria? Can bidders challenge the decision by the awarding authority in an independent tribunal?
- Are the cost-benefit assessments and the ranking of different projects of a tendering process made public?
- What dispute resolution mechanisms exist to ensure that disputes arising at any point in the lifetime of an infrastructure project are handled in a timely and impartial manner?

Source: OECD *Policy Framework for Investment* (2015).

Since then the government has implemented several reforms to improve the legal framework for infrastructure development. In particular, a new PPP Law was adopted on 31 October 2015 to provide a legal framework for co-operation between the state and business entities in delivery of PPP projects. This marks an important change in light of the OECD 2012 recommendations and considering that the private sector has repeatedly pointed to the inadequate legal framework as an important limiting factor for their participation.[41] The Law introduced several changes to the legal framework of Kazakhstan, amending and extending some of the provisions of the Law on Concessions, which is the principal source of rules governing concessions as described in Chapter 2.[42] For example, prior to the adoption of the PPP Law, PPP was defined in accordance with Article 19 of the Law on Concession as a form of co-operation between the state and private businesses aimed at financing, creating, reconstructing and (or) operating social and critical infrastructure; now, pursuant to the PPP Law, PPP can apply in any sector of the economy (Ernst and Young, 2015). In addition, several new terms have been defined in the Law (such as "public partner", "private partner", "PPP project"), while the main principles of balance, consistency, competitiveness and efficiency have been adopted from the Law on Concessions. The law also provides for an intended more robust institutional framework that includes a PPPs agency, the PPP Centre (established in 2008),[43] whereas the National Chamber of Entrepreneurs – Kazakhstan's umbrella business association – has been assigned a role in the implementation of PPP projects.[44]

To-date, no PPP project based on the new Law has been implemented, and investors appear to be awaiting the results from the first pilot project to assess the adequacy of the new legal framework.[45] Hence, currently, it is too early to assess the impact of the recent changes on the attractiveness of investment in infrastructure for private firms and their future willingness and ability to engage in infrastructure projects. Still, the cumulative effect of the various initiatives undertaken by the government over the years appears to be producing some results. As noted in Chapter 2, EBRD has been assessing positively the direction of the undertaken reforms and has substantially increased its investment in Kazakhstan in recent years, with nearly half of project portfolio being in infrastructure.[46] With several large scale projects planned for the coming years, within the Silk Road initiative and beyond,[47] the expectations are high, and it will be critical for the authorities to ensure that corruption and project delays do not hamper the realisation of these plans in practice.

Policy recommendations

Overall, while the WTO accession process marks a fundamental step in the country's trade policy reform, it addresses some, but not all, trade-related policy challenges in Kazakhstan. The long process of negotiation has led to

liberalisation of several barriers to FDI in services, and led to a reform of some elements of local content policies. The predictability of the country's trade regime has also likely improved, being now bound by common WTO rules and an international enforcement mechanism. To reduce meaningfully trade costs faced by firms and facilitate their participation in global markets, the government will, however, need to go further. This will involve a committed trade facilitation reform, further investment in physical infrastructure and economic co-operation with key trade partners, inside and outside of the region, via preferential trade agreements and regulatory co-operation. The progress in the latter area will mean not only a better access to foreign inputs by foreign firms investing in Kazakhstan but also better market access conditions for Kazakh firms abroad.

Trade policy

- *Build on the momentum from the WTO entry to engage in further trade reforms:* The WTO entry has marked an important step in the country's reform process. In some sectors Kazakhstan made limited commitments at the time of its WTO entry or opted for numerous transition periods and exceptions. The authorities could consider if further opening in some of these areas would not be beneficial. An offer to join the GPA could also be tabled swiftly.
- *Engage in further trade negotiations with countries where trade complementarity is high and no Free Trade Agreement exists.* Kazakhstan has thus far prioritised trade integration within the Eurasian Economic Union and with the European Union. Meanwhile, trade opportunities may also exist elsewhere (e.g. Iran) and signing further trade agreements could support the objectives of economic diversification.
- *Engage in further negotiations with the main trading partners to reduce non-tariff barriers (NTBs) to trade and intensify regulatory co-operation.* Regulations of other Eurasian Economic Union's members appear to be the main source of NTBs in Kazakhstan. Pursuing further regulatory co-operation within the Union would hence be beneficial, provided that new Union-level NTBs are not created that reduce trade opportunities with third countries.
- *Pursue ambitious trade facilitation reform to help reduce trade costs faced by all firms:* Being a remote and landlocked country, Kazakhstan relies on the efficiency of its border procedures and adequacy of its surface and air infrastructure for trade in non-oil products. Meanwhile, Kazakhstan scores significantly below the OECD average and the best performers in the region in this area, and previous customs modernisation plans have not been fully implemented.
- In particular, *streamlining and automating border procedures should be pursued further by the authorities* to help reduce trade costs faced by firms. While progress at the level of the Eurasian Economic Union will require diplomatic

solutions, better oversight internally may also be required. A Time-Release Study can help the government identify the most acute bottlenecks, prepare a detailed action plan and allow for better monitoring of progress in practice. It can also provide a basis for engaging in targeted capacity-building programmes with relevant organisations and donors (e.g. WCO, the EU).

Infrastructure investment

- *Build stronger PPP capacities within the government*. With the enactment of a new PPP law, Kazakhstan should not underestimate the importance of well-trained professionals able to manage complex tender offerings and risks linked to large-scale infrastructure projects.
- *Strengthen integrity frameworks* relating to infrastructure investment, including conflict of interest and the procurement system.
- *Ensure that the pilot PPP project does not suffer from irregularities and project delays:* Many investors await the implementation of the first pilot PPP project to assess the adequacy of the new regulatory framework for PPPs. The authorities are advised to pay particular attention to project's implementation to send the right signal to the investors.

Notes

1. See Jensen and Tarr (2007). The sectors that benefit and expand most are those that export the largest share of their output (e.g. electrical equipment, chemicals, oil and gas, basic metals and communications equipment) while those that are most protected or export little, contract most (e.g. medical equipment, wood products, vehicles, non-metal products and publishing (Jensen and Tarr, 2007: 25). The study uses a static computable general equilibrium (CGE) model covering 56 economic sectors and using small open economy assumptions and accounting for Dixit-Stiglitz variety-productivity effects in downstream sectors. The authors have applied a similar model to assess the effects of Russia's entry to the WTO (Jensen, Rutherford and Tarr, 2007) and found similar results (in case of Russia, they predicted the gains to amount to 3.3% of Russia's GDP). Besides Jensen and Tarr (2007), there are several other studies that aim to quantify the overall economic welfare gains from Kazakhstan's WTO accession (e.g. World Bank, 2013; World Bank; 2015). They rarely model the effect of local content policy reforms, usually measuring the effect of reduction in tariffs only, at times taking into account the likely effect of a complementary trade facilitation reform (e.g. World Bank, 2015).
2. Kazakhstan's President signed on 12 October 2015 the Law No. 356-V "On ratification of the Protocol on accession to the Marrakesh Agreement as of April 15, 1994", which was first approved by both chambers of the Parliament. Subsequently, the government has officially notified the WTO about the completion of the ratification process, and on November 30 Kazakhstan became the 162nd WTO member. For the WTO press release: *www.wto.org/english/news_e/news15_e/acc_kaz_30nov15_e.htm*.

3. For more information on the WTO DSM, see: *www.wto.org/english/thewto_e/whatis_e/tif_e/disp1_e.htm*.
4. WTO (2015a: §0896-97; §0933-0934; §0945-0950).
5. For example, the limit on foreign staff among managers and specialists still remains as the total number of foreign managers and specialists hired as ICTs must not exceed 50% (see WTO, 2015c: 5).
6. See WTO (2015c: 30).
7. See WTO (2015a: §0896-97).
8. See WTO (2015a: §0933-0934).
9. See WTO (2015c: 30).
10. Law No. 422-V "On amendments and addenda to certain legislative acts of the Republic of Kazakhstan on the issues of non-performing loans and assets of the second-tier banks; on rendering financial services and activities of the financial institutions and the National Bank of the Republic of Kazakhstan" of 24 November 2015.
11. The agreed bound tariff levels of Kazakhstan are reflected in the country's Schedule of Goods, which forms a part of its Accession Package. See WTO (2015b).
12. This phenomenon has been documented in several earlier publications. See, for example, Shepotylo (2011), Jandosov and Sabyrova (2011), World Bank (2012) and World Bank (2015).
13. The EurASEC lasted between 2000 and 2014 and comprised of Belarus, Kazakhstan, the Kyrgyz Republic, Russia and Tajikistan. It was established on 10 October 2000 and terminated on 31 December 2014 (in order to be replaced by the EAEU on 1 January 2015).
14. The Treaty on the Establishment of the Common Customs Territory and Formation of the Eurasian Customs Union came into force on 1 January 2010.
15. By the end of 2010, the customs duties collected on goods originating outside the CU were distributed according to an agreed formula of 4.70% for Belarus, 7.33% for Kazakhstan and 87.97% for Russia.
16. WTO Agreement on the Implementation of Article VII of the GATT 1994, i.e. WTO Customs Valuation Agreement.
17. According to the government, Kazakhstan has fully implemented the WTO Agreement on Customs Valuation during the process of accession to the WTO. For instance, Articles 4.3 and 4.4 of the Agreement on the Determination of Customs Value of Goods, Transferred Across Customs Border of the Customs Union of 25 January 2008 were amended as of 10 October 2014. Pursuant to the changes, declarants were provided an opportunity to demonstrate two different means of establishing the acceptability of a transaction value: examination of the circumstances surrounding the sale and demonstration by the declarant that the transaction value closely approximated a "test value" previously accepted by the customs body. Furthermore, the Commission jointly with EAEU member States adopted several documents that incorporated the remaining provisions of the Interpretative Notes.
18. GATT 1994 (Article XI)
19. In the past the government undertook measures that had a conflicting impact on price formation and trade opportunities by firms in certain sectors. For example, while introducing temporary bans on grain exports, the government continued providing a transport subsidy for grain exporters (OECD, 2013).

20. The Strategic Plan of the Ministry of Finance 2011-2015 outlined a customs modernisation plan.

21. According to the authorities, several elements of a Single Window for Trade have been implemented throughout the 2011-13 period (pursuant to the government plan enshrined in the Government Resolution No. 771 of 3 July 2011). Still, several elements are lacking or require significant improvements. Currently, there is work planned to create a Single Window for Trade at the level of the ECU for the period 2015 to 2020, which will impact the progress in this area.

22. While the status of an AEO is enshrined in the ECU's Customs Code, the operationalization of the programme has proven challenging. As of 2015, there have been no firms in Kazakhstan that benefitted from the AEO status.

23. Electronic declaration is in the process of being implemented in the context of the government's collaboration with UNCTAD on customs modernisation. A pilot system is planned to be implemented in July 2016 and the full ASYCUDA system should be implemented by July 2017. Electronic payment is currently not integrated into the automated declaration processing system even though such plans exist within the plan of implementing electronic declaration system. The self-diagnosis undertaken by the government of Kazakhstan stipulates that several legal changes will be required as well as better intra-governmental coordination, improved the functioning of the available IT systems, and provision of training and capacity building for agencies and staff involved to achieve such integration in practice.

24. Article 23 of the Customs Code of Kazakhstan (currently under revision) together with the Order of the Minister of Finance No. 244 and 501 and the Agreement on Mutual Administrative Assistance of the Customs Bodies of the Customs Union Member States of 21 May 2010 (Law No. 311-IV of 30 June 2010) provide a legal basis for the application of automated customs risk management system. However, the system, in place since 2010, is still rudimentary and applied by Customs only (and no other border agencies). For example, UNECE (2014) reports that at certain customs points, all commercial traffic is physically inspected.

25. For example, in 2015, the government entered collaboration with UNCTAD to help modernize its customs procedures, including to align its regulations with the WTO TFA and other international standards as well as to implement the integrated customs management system ASYCUDA. The co-operation is planned for 2016-20, and the ASYCUDA system should be implemented by July 2017. For more information, see *http://unctad.org/en/pages/newsdetails.aspx?OriginalVersionID=1174&Sitemap_x0020_Taxonomy=UNCTAD%20Home*.

26. The diagnostic has been undertaken by the Kazakhstan's government (Ministry of National Economy) in collaboration with UNECE and UNCTAD between October 2014 and January 2016.

27. For example, the Strategic Plan of the Ministry of Finance (2011-15) already outlines the customs modernisation plan albeit it is unclear what results were achieved in practice.

28. For example, exporters and importers of some products (e.g. certain seeds, metal sheets, electric motors) are all required to submit more than 10 supporting documents in Kazakhstan in order to make a cross-border shipment, each of which can take a dozen days to obtain (UNECE, 2014).

29. According to UNECE (2014), the EAEU regulations are a predominant source of NTBs in Kazakhstan (52.6%), followed third-country regulations (34.9%) and domestic regulations (12.4%).

30. For example, the World Bank (2015: 17) stipulates that some regulatory changes required by EAEU internal integration, e.g.: i) issuance of more stringent regulations; ii) excessive mandatory certifications; iii) new state product registration requirements; iv) new requirement of registering third country suppliers; and v) prevalence of quantitative controls; have led to imposition of new NTMs and may lead to trade diversion.

31. Article X(1) of GATT 1994, Article III of General Agreement on Trade in Services (GATS) and Article 63 of the Agreement on Trade Related Aspects of Intellectual Property (TRIPS).

32. See §1146-1148, §0208 and § 0250 in WTO (2015a). §0250 clarifies specifically that the ECU Commission Decision No. 308 of 18 June 2010 had been amended to establish and put into effect a mechanism for publication of proposed EAEU legal acts before their adoption and to provide reasonable period of time for Members and interested parties to provide comments to the competent EAEU bodies.

33. Several WTO agreements impose specific notification requirements on WTO members, e.g. regarding notification of the use of relevant subsidies or TRIMs, as covered by the ASCM and TRIMS agreements. In addition, §1149 and 1150 of Kazakhstan's WTO Accession Protocol stipulate that Kazakhstan is to submit all initial notifications by the time of its accession; the remaining notifications according to the timetable outlined in Table 4 of the Protocol, and all subsequent notifications in conformity with relevant WTO provisions.

34. See §0209 in WTO (2015a).

35. See WTO (2015a: §1132-1134).

36. For example, all licensing requirements and procedures must be set out in normative acts and any law establishing or implementing them needs to be published prior to its effective date. The relevant authorities need to review and make a decision on granting or denying a licence within the period specified in official procedures or, if no time period was specified, without undue delay. For a full list of commitments in this area, see WTO (2015a: §1132).

37. See WTO (2015a: §1133).

38. Since the establishment of the WTO and 2008, there have been at least 20 cases involving consideration of Article of the GATT Agreement (Ala'i, 2008: 789), which represents 5% of all cases submitted during that period, as recorded by the WTO website.

39. See e.g. Vinokurov et al. (2015), World Bank (2015a), World Bank (2015b), Knobel et al. (2016).

40. The EPCA has by now been ratified and came into force as of 1 May 2016.

41. The scope of the dispute settlement mechanism is outlined in Chapter 14 of the Agreement and Article 160. All provisions of the Agreement, except for Articles 156, 158, 159(3) and (4), are subject to the mechanism.

42. See e.g. Roundtable on some aspects of public-private partnership development in Kazakhstan, available at *www.ey.com/KZ/en/Industries/Government---Public-Sector/View-on-PPP-in-Kazakhstan*.

43. The July 2006 Concession Law No. 167-III, as amended (the "Concession Law"). See Chapter 2 for an assessment of the Concession Law.

44. The PPP Development Centre's mandate is to evaluate concession/PPPs deals and to recommend further improvements in PPPs (As established by Government Resolution No. 693 dated 17 July 2008 "On Establishment of a specialised

organisation on concessions"). It is involved in all stages of the process, including appraisal of contracts, feasibility studies, assessment of concession applications submitted for tenders, consideration of state guarantees for individual concessions and co-financing by the state budget and the monitoring of concession projects. For more information, see the Centre's website: *www.kzppp.kz*.

45. Pursuant to the National Chamber Law dated 4 July 2013, the Chamber's mandate is to ensure favourable legal, economic and social conditions for business initiatives and to promote a mutually beneficial partnership between the business community and Kazakhstan government authorities. Accordingly, for example, potential private partners shall be selected from the Register of Potential Private Sector Partners maintained by the Chamber.

46. Information obtained through consultations of the OECD Secretariat with business stakeholders in Kazakhstan in 2015-2016. The first major PPP project in Kazakhstan involves construction and operation of light rail line in Almaty with the estimated project cost of USD 521 million, construction period of 2 years (2016-2018) and operation period of 27.5 years. In July 2016 the project was at the stage of preparation of a concession proposal. For more information, see PPP Centre's website (*www.kzppp.kz*).

47. EBRD's investment in Kazakhstan increased from EUR 328 million in 2013 to EUR 790 million in 2015 (i.e. increase of 141%). The current project portfolio (of EUR 2,455 million) comprises of infrastructure projects (44%), energy (41%), industry, commerce and agribusiness (11%) and financial institutions (4%). See EBRD (2016).

48. According to the Ministry for Investments and Development's Committee on Highways, USD 4.2 billion (1.5 trillion KZT) were allocated in 2015 to support domestic transport. In addition, several large infrastructure investment projects are planned with the participation of Chinese investors within the Silk Road initiative; including a dry port on the China-Kazakh border (Khorgos Gateway); three railways (including one high speed railway from Moscow to Kazan) and two gas pipeline projects. For more information, see the Ministry for Investments and Development website (*www.mid.gov.kz*).

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WTO (2015b), *Schedule of Goods*, WT/ACC/KAZ/93/Add.1.

WTO (2015c), *Schedule of Specific Commitments in Services*, WT/ACC/KAZ/93/Add.2.

ANNEX 6.A1

Description of Kazakhstan's WTO commitments in the services sector

Kazakhstan has made specific commitments in ten services sectors, and 116 sub-sectors, under its Schedule of Commitments under the WTO General Agreement on Trade in Services (GATS). Some of them horizontal in nature – affecting two or more services sectors – while other sector-specific. They are described in more detail below and summarised in Table 2.1 in Chapter 2.

Horizontal commitments

Regarding restrictions on hiring **key foreign personnel**, Kazakhstan has made specific commitments, in its WTO Services Schedule, in relation to the entry and temporary stay of business persons and intra-corporate transfers (ICT) of executives, managers and specialists.[48] For example, the total number of ICTs is limited to 50% of the total number of foreign managers and specialists within each service supplier, with the minimum of three individuals, while the corresponding shares are 70% and 90% for other categories of foreign employees.[1] The entry and temporary stay of ICTs should be permitted for 3 years, subject to certain conditions[2], and can be extended for another year, on the basis an economic needs test (ENT). In addition, after the expiry of the five-year transition period after the country's WTO entry, an ENT shall not apply for hiring ICTs as managers and specialists.[3] Business visitors[4], in turn, can also enter and remain in Kazakhstan without obtaining a work permit for a period not exceeding 90 days. Still, despite these commitments, restrictions on key personnel remain important in Kazakhstan and will remain to be reflected in Kazakhstan's scores on the FDI Index even once all WTO commitments are fully implemented.

Kazakhstan has also undertaken several specific commitments relating to its use of **local content policies**, as predicted at the time of the previous *Investment Policy Review* (OECD, 2012: 40). For example, from the date of its accession to the WTO, Kazakhstan is required to ensure that all laws, regulations and other measures applied in Kazakhstan, which are within the

scope of the TRIMs Agreement, would be consistent with the relevant WTO provisions, including the TRIMs Agreement, whether adopted by Kazakhstan or the competent bodies of the EAEU, except in the Subsurface and automotive sectors.[5] In the case of automotive and subsurface sectors exceptions and transition periods apply.[6] However, even in these sectors, Kazakhstan will not be able to include any provisions that are WTO-inconsistent in the newly concluded contracts (nor include them in the signed contracts that are being renewed).[7] In addition, government committed not to require more than 50% of local content in services from investors in the subsurface sector.[8] When a tender procedure is used for services procurement, investors shall, for a period of six years, consider a putative 20% reduction in the price of any bid submitted by a juridical person of Kazakhstan where at least 75% of that subcontractor's qualified employees[9] are citizens of Kazakhstan (to be reduced to 50% after six years), provided that the subcontractors meets the standards and qualitative characteristics stipulated in the tender documents.[10] The government also committed not to adopt any local content measures in the sector that exceeded the measures provided for in Law No. 291-IV "On Subsurface and Subsurface Use" of 24 June 2010, as applied in September 2011, and clarified the method for calculating local content.[11]

This language and the extent of commitments are similar to the type of commitments that certain recent WTO adherents have committed to in their Accession Protocols, such as the Russian Federation (in 2012) or China (2001).[12] The principal basis for such commitments and the WTO rules on local content stems from the TRIMs Agreement[13] as well as relevant provisions in GATS, the SCM Agreement; and the GPA. To-date, there have been 34 disputes relating to local content policies in WTO, quoting various WTO provisions, including the TRIMs Agreement, GATT, GATS, and the SCM Agreements), which means that, in case of non-compliance, Kazakhstan may face a risk of potential disputes with other WTO members.[14] The use of local content is also prohibited in some Bilateral Investment Treaties and Free Trade Agreements that Kazakhstan had entered. Given these commitments, the government, as seen in Chapter 2, has amended its Subsurface legislation to stipulate that i) new investment contracts in the sector cannot include any local content provisions related to the purchases of goods, and ii) local content in works and services shall not exceed 50%.[15] The law continues to grant a conventional 20% discount to Kazakh entities providing works and services to Subsurface users when a tender procedure is applied; and excludes preferences provided to domestic producers of goods, works and services participating in procurement tenders of quasi-state entities.

When it comes to **access to land**, Kazakhstan has made no commitments in relation to restrictions on private ownership of land used for farming, agricultural production and forest planning (while no restrictions exist on other forms of land).[16] Hence, the currently applied maximum rental period of

10 years does not need to be extended as a result of the WTO entry. As noted in Chapter 2, such short lease period may pose a barrier to investment in commercial agriculture sector and the associated services in Kazakhstan. While the government planned to extend the lease period, the reform has been stalled due to public protests.

Sector-specific commitments

In **telecommunications**, WTO entry has already brought about a reduction in the level of restrictions: Kazakhstan has committed to remove the foreign equity limits in the sector within 2.5 years following the country's WTO accession (except for JSC *Kazakhtelecom*) and already removed the limit at the start of 2016 (see Chapter 2). The WTO commitment will also prevent the government from reinstituting the previous maximum equity restriction, once the transition period expires. Still, other regulatory barriers to market entry for both foreign and domestic operators persist in the sector, which are not be covered by the WTO GATS or other related commitments, and may limit de facto investment and trade opportunities in the sector post WTO entry.[17]

Transport is another sector where Kazakhstan has had a relatively high level of restrictions on foreign entry prior to WTO entry.[18] However, Kazakhstan made few limited commitments in the sector.[19] Notably, it did not commit to remove the foreign equity limit (of 49%) in the air transport sector. Commitments in other transport sectors have been limited too. For example, the local incorporation requirement in maritime transport has not been removed, and the requirement to register vessels in Kazakhstan has remained unbound.[20] Beyond the changes related to removal of any horizontal restrictions, Kazakhstan's score on the FDI Index in the sector will hence not change as a result of WTO entry. Still, as described in Chapter 2, the country has recently undertaken liberalisation, removing the equity limit. Allegedly, during the summer of 2016 a new law was in the process of being drafted, which would, if passed, reinstitute the previous restriction. The lack of WTO commitments in this area means that such changes could occur in the future.

Finally, **financial services** are a third services sector in which restrictions on foreign entry were relatively high in Kazakhstan compared to the OECD average (Kazakhstan's score of 0.183 is five times higher than the OECD average in 2014), and will require changes upon WTO entry. Currently, foreign banks and insurance companies may open a representative office with permission of the National Bank of Kazakhstan (NBK) but may not open branches (see Chapter 2). Within its WTO accession, Kazakhstan committed to allowing foreign banks and foreign insurance companies to open branches within 5 years after accession (i.e. by 2020). In addition, there are certain provisions relating specifically to the issuance of licenses for companies operating in the financial

services sector enshrined in Kazakhstan's broad commitments on licensing requirements.[21] Still, even after the expiry of the five year transition period, certain limitations will apply both in the insurance and banking sectors[22] and other specific restrictions will apply to the re-insurance services.[23] Still, this is one area where WTO commitments will imply further future liberalisation, and lead to reduction of scores on the OECD FDI Index.

Notes

1. See WTO (2015c: 3-6).
2. See WTO (2015c: 5).
3. "The entry shall be permitted for three years, based on the permits, annually issued by the authorized body, provided that the company fulfils one of the following requirements: i) offer training, retraining or advanced training programs for their Kazakhstani employees in skills necessary for subsequent replacement of foreign workforce, or ii) create additional jobs for Kazakhstani employees. The above stated categories of persons must have at least one year work experience in a company, which represents a juridical person of another Member and within which they are being transferred to Kazakhstan". WTO (2015c: 5-6).
4. See WTO (2015c: 4).
5. Business visitors mean persons who are not domiciled within the territory of Kazakhstan and are representatives of a service supplier of the WTO Member and entering the territory of Kazakhstan in order to conduct negotiations on sales of services of this supplier, enter into agreement on sales of services, participate in business meetings or establish commercial presence of a service supplier, and are not engaged in making direct sales to the general public or in supplying services themselves nor receive remuneration from a source within Kazakhstan.
6. WTO (2015a: §0896).
7. In case of contracts between the state and an investor in the Subsurface sector and industrial assembly agreements in the automotive sector that were signed prior to 1 January 2015, all TRIMs-inconsistent measures need to be removed by 1 January 2021 and 1 July 2018, respectively, or by the time of the expiry of the initial duration of the contract, whichever comes sooner. See WTO (2015a, §0897).
8. See WTO (2015a: §0896). All WTO-inconsistent measures included in contracts signed with investors in the automotive and Subsurface sector prior to 1 January 2015 would cease to be enforced by1 July 2018 and 1 January 2021, respectively. Kazakhstan is also obliged to engage in consultations with interested WTO members regarding the new WTO-consistent measures that will be applied instead in those two sectors by no later than 1 July 2019 and 1 January 2019, respectively; as well as notify WTO members of any measures planned to replace the currently applied measures at least six months prior to their adoption.
9. In addition, even if a potential investor might have offered a level of Kazakhstan content for personnel or services above 50%, the Government shall not take it into account when determining the tender winner for purposes of granting subsurface use rights. WTO (2015a, §1127)

10. Qualified employees mean executives, manager and specialists as defined in Kazakhstan's commitments on intra-corporate transfers in its Schedule of Services (WTO, 2015c: 3)

11. See WTO (2015c: 2-3).

12. See WTO (2015a, §1127). Kazakhstan content of personnel in the Subsurface sector would be calculated as the proportion (on a per capita basis) of executives, managers and specialists who were citizens of Kazakhstan; and Kazakhstan content in all services rendered to the investor would be defined as the share of the total annual amount of payments (expenditures) for services under all contracts that were paid to juridical persons of Kazakhstan. In the case of Kazakhstan's content in all services rendered to the investor, the amount paid to juridical persons of Kazakhstan would, however, be reduced by any amount paid for services that were performed by enterprises that were not juridical persons of Kazakhstan.

13. Since the relatively recent accession of the Russian Federation to the WTO, already several WTO disputes have arisen quoting the country's alleged breach of the provisions under *the TRIMs Agreement*. For example, the WTO case DS462 submitted by the European Union against the Russian Federation and the case DS463 submitted by Japan quote the alleged breach of Article 2.1 and 2.2 of the *TRIMs Agreement*. Both cases are on-going and have not yet resulted in a ruling on the subject.

14. The TRIMs Agreement specifically provides that no Member shall apply measures that are inconsistent with Article III of GATT (on national treatment) and Article XI of GATT (on quantitative restrictions) through an application of measures that are "mandatory or enforceable under domestic law or under administrative rulings, or compliance with which is necessary to obtain an advantage, and which require: a) the purchase or use by an enterprise of products of domestic origin or from any domestic; source, whether specified in terms of particular products, in terms of volume or value of products, or in terms of a proportion of volume or value of its local production; or b) that an enterprise's purchases or use of imported products be limited to an amount related to the volume or value of local products that it exports." See the WTO TRIMs Agreement, Article 2 and the illustrative list of measures in the Annex.

15. According to the WTO, issues relating to the alleged inconsistency of certain measures with the *TRIMs Agreement* have been raised in 34 requests for consultations under the DSU, 16 of which have moved to the establishment of a panel, 6 have been settled or terminated through a mutually agreed solution, and the remainder is currently in consultation. In addition, a number of cases have referred to other WTO provisions and concluded in the ruling. For example, in the case DS139 (*Canada-Autos*), Article 3.1(b) of the SCM Agreement was found to prohibit both de jure and de facto local content-contingent subsidies; and several cases relating to the use of local content in the energy area have referred to the relevant provisions in the GATT, TRIMs and SCM Agreements (e.g. DS412, DS426, DS452, DS456). For a discussion of this issue, see for example Bohanes (2015).

16. Law No.365-V "On the Introduction of Amendments and Additions to Certain Legislative Acts of the Republic of Kazakhstan with Respect to the Accession to the World Trade Organisation" of 27 October 2015 that came into force on 9 November 2015.

17. See WTO (2015c: 3).

18. For example, cross-ownership among incumbent firms limit competition in the domestic market and incumbent operators have long exclusivity rights in such areas

as long-distance and international services and interconnectivity for mobile operators, for example. This has resulted in relatively low competitiveness of the sector, whereby the costs of long distance telephone services and broadband internet access are three to six times higher than in comparator countries such as Russia, selected EU countries, and can serve as a break on the competitiveness of local firms (Jensen and Tarr, 2008: 4). Hence, in order to help attract investment and ensure level playing-field between different operators in the sector, further regulatory changes in the area of competition, corporate governance and sector-specific regulations will be required (see Chapter 2 and the section on competition policy in this chapter).

19. Kazakhstan has an average score of 0.325 in the transport sector on the FDI Index (i.e. about two times higher than Kazakhstan's overall FDI Index score and the OECD average in that sector). Air transport is also the second most restrictive sector in Kazakhstan, after fixed telecommunications.

20. See section 11 in the Schedule of Specific Commitments in Services (WTO, 2015c: 28-33).

21. See WTO (2015c: 28-31).

22. Kazakhstan's relevant regulatory authority is to make an administrative decision on a completed application for issuance of a licence and authorization for the supply of a financial service, and, if appropriate, approval of new products and rate changes, within a reasonable period of time, and would promptly notify the applicant of the decision. Where it was not practicable for a decision to be made on: i) an application for supply of banking services to receive an authorization within six months, and to receive a licence within two months; and, ii) an application for supply of other financial services to receive an authorization within three months, and to receive a licence within one month, the relevant regulatory authority would notify the applicant without delay. See WTO (2015a), §1132.

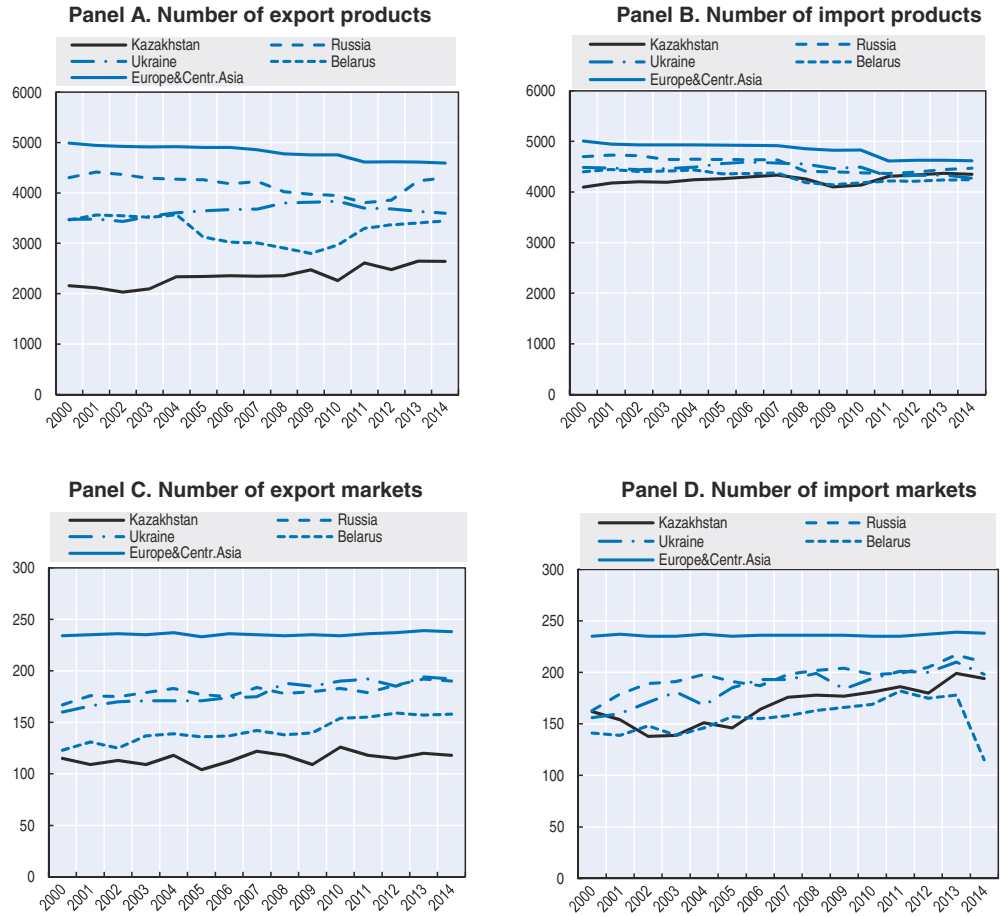
23. The minimum amount of total assets of the non-resident insurance company, which has filed in an application to open a branch, must amount not be less than USD 5 billion; the experience of the parent insurance company of non-resident insurer should be at least 10 years, and the day-to-day activity of the branch should be manage by at least two residents of the Republic of Kazakhstan. See WTO (2015c: 18-19). The minimum amount of total assets of the non-resident bank, which has submitted the application for opening of a branch, must be not less than 20 billion US dollars, and the minimum amount of deposit, which can be accepted from natural persons by foreign bank branches must be not less than 120,000 US dollars; and the day-to-day activity of the branch should be manage by at least two residents of the Republic of Kazakhstan. WTO (2015c: 22)

24. The total amount of insurance premiums paid by the cedent company to reinsurance companies-non-residents of the Republic of Kazakhstan shall not exceed 85% of the total amount of insurance premiums received by the cedent (including premiums paid to reinsurance companies) at the end of the full financial year. This limitation shall not apply to the risks related to maritime transportation services (except for vessels supplying solely or permanently cabotage transportation services) and commercial aviation and space launching and freight (including satellites), with such insurance to cover any or all of the following: the goods being transported, the vehicle transporting the goods and any liability arising therefrom. See WTO (2015c: 19).

ANNEX 6.A2

Overview of Kazakhstan's trade structure

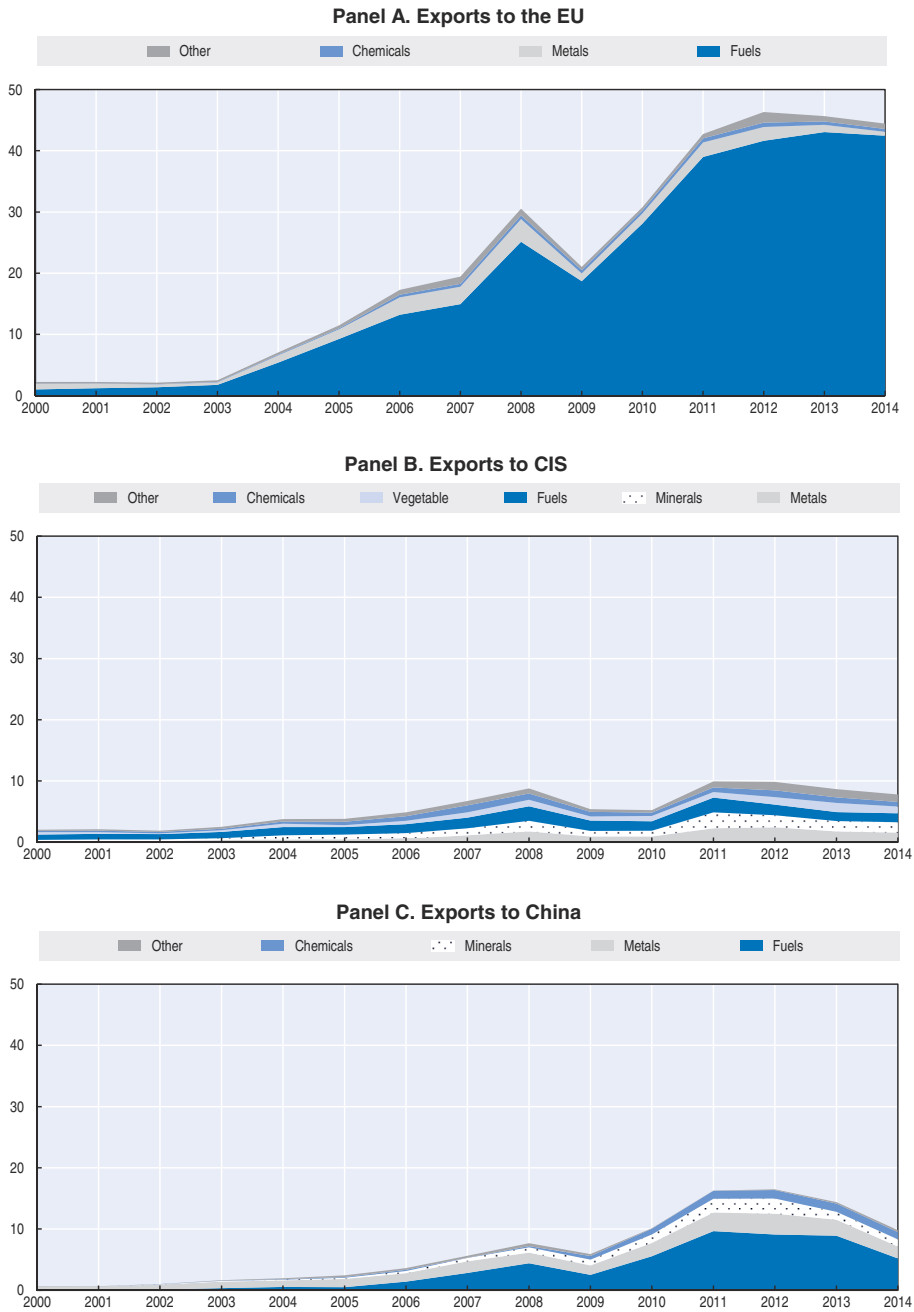
Figure 6.A2.1. **Number of export and import products in Kazakhstan and comparator economies, 2000-14**



Source: WITS database.

StatLink http://dx.doi.org/10.1787/888933453018

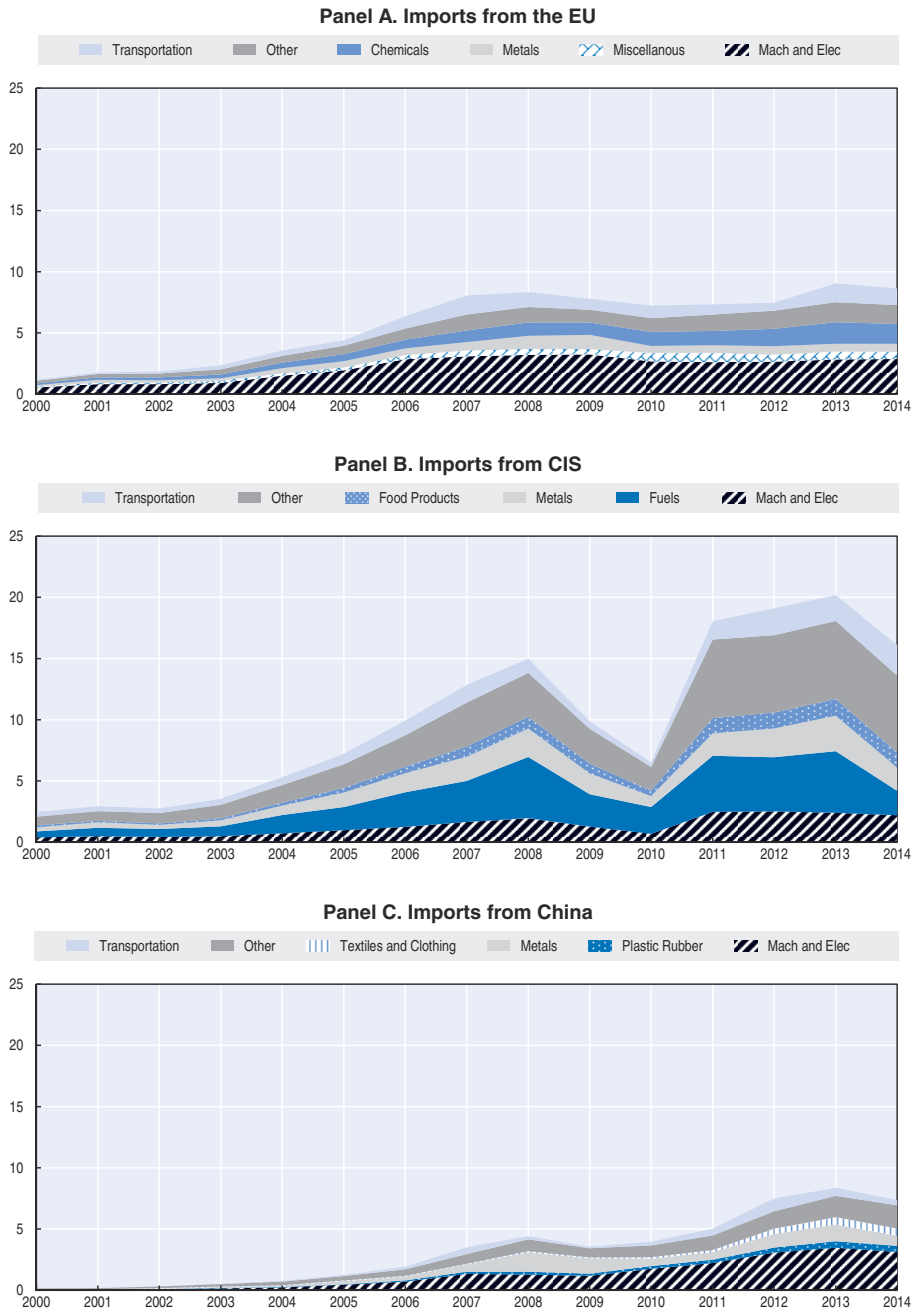
Figure 6.A2.2. **Kazakhstan's export structure with the main trading partners, 2000-14**



Source: UN COMTRADE.

StatLink http://dx.doi.org/10.1787/888933453029

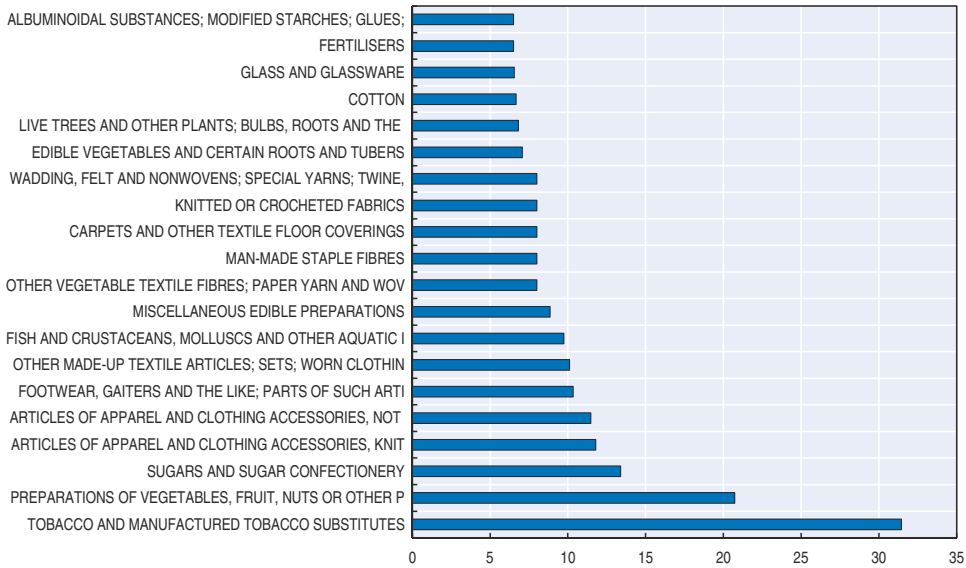
Figure 6.A2.3. **Kazakhstan's import structure with the main trading partners, 2000-14**



Source: UN COMTRADE.

StatLink http://dx.doi.org/10.1787/888933453039

Figure 6.A2.4. **Top twenty Kazakh export products with the highest applied import tariff in the EU, 2015**



Source: Authors' calculations using the UN TRAINS database.

StatLink http://dx.doi.org/10.1787/888933453044

Table 6.A2.1. **Average EU import tariffs applied on Kazakh exports and the value of affected Kazakh exports, 2015**

	Average applied tariff	Value of exports (in bln USD)	Share in exports (in %)
WTO HS Petroleum	2.34	28.74	92%
WTO HS Industrial	3.92	2.07	7%
WTO HS Agricultural	5.28	0.27	1%
Total Trade	4.02	31.09	100%

Note: Product groups are based on standards WTO HS product classification.
Source: Authors' calculations using the UN TRAINS database.

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Chapter 7

Responsible business conduct in Kazakhstan and the OECD Guidelines for Multinational Enterprises

Responsible business conduct (RBC) is an important part of the investment climate and is increasingly integrated within policies aimed at attracting better quality investment and enhancing sustainable development. In line with global trends, RBC has also emerged as an important topic in Kazakhstan. Kazakhstan's adherence to the Declaration, and, in particular, the establishment of a National Contact Point for the OECD Guidelines for Multinational Enterprises, is an opportunity to further promote RBC principles and standards, both within the government and with the wider public, and to further clarify and set out the government's expectations on RBC.

While Kazakhstan continues to open its policy regime for trade and investment and improve the business environment to attract more investment, it also needs to maximise the positive impact of investment, leveraging the OECD *Guidelines for Multinational Enterprises* (*Guidelines*), a commitment by each country that adheres to the *Declaration on International Investment and Multinational Enterprises* to promote and enable responsible business conduct (RBC). This chapter reviews Kazakhstan's policies in this area, including the planned institutional arrangements for establishing a National Contact Point (NCP) for the *Guidelines* based on the recommendations from the 2012 OECD *Investment Policy Review of Kazakhstan* (see Box 7.1). The chapter also takes into consideration the increasing global policy attention given to RBC in improving the business climate (see Box 7.2).

Box 7.1. **2012 Recommendations on responsible business conduct by the OECD**

- Put in place a coherent government strategy for facilitating responsible business conduct.
- Expand disclosure requirements for enterprises to include environmental and other non-financial performance.
- Encourage due diligence for responsible supply chains of minerals. In light of the importance of the mining sector in Kazakhstan and development of the country's outward investment projects in the region, the government might consider endorsing and encouraging dissemination among companies of the OECD Due Diligence Guidance for Responsible Supply Chains of Minerals from Conflict-Affected and High-Risk Areas.
- Consider creating an institution capable of fulfilling the role of promoting responsible business conduct similar to that of National Contact Points for the OECD *Guidelines for Multinational Enterprises*.

Source: OECD, 2012.

Box 7.2. **International convergence and coherence on RBC**

The consensus built around the 2011 update of the OECD *Guidelines for Multinational Enterprises* and the unanimous endorsement of the UN Guiding Principles on Business and Human Rights by the UN Human Rights Council has brought about international convergence and coherence on what responsible business conduct entails. The result has been a clearer understanding of the baseline standards for how businesses should understand and address the risks related to the actual and potential impacts of their operations, and how governments should support and promote responsible business practices. This common understanding has contributed to creating a more predictable business environment.

This coherence is echoed in other international standards, including the ISO 26000 Guidance on Social Responsibility, the IFC Performance Standards, and the OECD Recommendation on Common Approaches for Officially Supported Export Credits and Environmental and Social Due Diligence, as well as, increasingly, regional and country strategies. For example, the European Union Corporate Social Responsibility Strategy and the United States National Action Plan on Responsible Business Conduct are based on the OECD Guidelines and the UN Guiding Principles. Many countries are also developing National Action Plans to ensure that the recommendations from governments on responsible business conduct are actually implemented on the ground. Finally, more and more countries are using responsible business conduct principles and standards to frame domestic law. For example, the United States Dodd-Frank Act specifically addresses due diligence for human rights along the minerals supply chain and requires companies to report on whether they source certain minerals (tin, tantalum, tungsten and gold) from conflict areas. Another notable development is the 2015 G7 Leaders' commitment to support responsible supply chains and improve access to remedy.

Understanding responsible business conduct

Responsible business conduct is a key element of a healthy business environment – one that attracts quality investment, minimises risks for businesses, ensures stakeholder rights are respected and ultimately leads to broader value creation. Irresponsible business practices erode the overall quality of the business environment; can result in large losses for businesses, environmental degradation, and poor conditions; and, in the most serious of cases, the loss of human life (see Box 7.3).

All businesses – regardless of their legal status, size, ownership structure or sector – should behave responsibly. As set out in the internationally recognised principles and standards on RBC, such as the *Guidelines* and the UN *Guiding Principles on Business and Human Rights* (UN *Guiding Principles*), this entails making

Box 7.3. **Responsible business is good business**

RBC can contribute to reducing costs and avoiding legal liability. In one study, nearly 20% of the 2,500 sampled companies were found to be subject to sanctions related to their social or environmental performance between 2012 and 2013, amounting to penalties upwards of EUR 95.5 billion (Vigeo, 2015). Likewise, a recent Harvard University study found that for a mining project with capital expenditure between USD 3-5 billion the costs attributed to delays from community conflicts can be on average USD 20 million per week due to lost productivity from temporary shutdowns or delays (Davis and Franks, 2014). RBC can also lead to increased returns, lower cost of capital, and higher employee retention. One study found that better business practices have the potential to reduce the cost of debt for companies by 40% or more and increase revenue by up to 20% (Rochlin et al., 2015). More broadly, a cross-sector study tracking performance of companies over 18 years found that high sustainability companies – that is those with strong environmental, social, and governance (ESG) systems and practices in place – outperform low sustainability companies in stock performance and real accounting terms (Eccles et al., 2011).

Suppliers of multinational enterprises (MNEs) may find that following RBC principles and standards gives them an advantage over businesses that do not, as they are able to respond to and address concerns that may come up in due diligence of the MNE when evaluating risks associated with its supply chain. Investors from the countries that adhere to the *Guidelines* are subject to them wherever they operate, including throughout the supply chain and in relation to business relationships. This means that a large majority of the global supply chain is covered by the *Guidelines* as these investors account for 75% global foreign direct investment (FDI) outflows and 58% of global FDI inflows between 2010 and 2015, as well as 81% of global FDI outward stock as of end 2014 (OECD/IMF, 2016). Similarly, businesses that want to access markets of these countries are also subject to the *Guidelines*, and, in some cases, actual regulation related to RBC.

a positive contribution to economic, environmental, and social progress of the countries in which they operate, while at the same time avoiding and addressing adverse impacts of business activities. RBC principles and standards emphasise the integration and consideration of environmental and social issues into core business operations. A key element of RBC is risk-based due diligence, a process through which businesses identify, prevent and mitigate actual and potential adverse impacts, and account for how these impacts are addressed. RBC expectations extend to business activities throughout the entire supply chain and linked to business operations, products or services by a business relationship. RBC is a term sometimes used interchangeably with

corporate social responsibility (CSR), although RBC is understood to be more comprehensive and integral to core business than what is traditionally considered CSR (mainly philanthropy).

Governments have a primary duty to protect the public interest and ensure that stakeholder rights are respected – they have an important role in promoting and enabling RBC. The RBC chapter in the OECD *Policy Framework for Investment* is a useful reference for designing and implementing a strong RBC policy framework. This entails establishing and enforcing an adequate legal framework that protects the public interest and underpins RBC, while monitoring business performance and compliance with the law. Setting and communicating clear expectations on RBC and providing guidance on what those expectations mean is important, while encouraging and engaging industry and stakeholders in collective initiatives and providing recognition and incentives to businesses that exemplify good practice is encouraged. Alignment of policies relevant to RBC is also important as is ensuring that, in the context of the government's role as an economic actor, RBC principles and standards are observed. Not only is this in the public interest, it also enhances the government's legitimacy in making recommendations on RBC to businesses (OECD, 2015a).

Understanding the OECD Guidelines for Multinational Enterprises

Addressed by the adhering governments to businesses operating in or from their jurisdictions, the *Guidelines* set out principles and standards in all major areas related to RBC, including information disclosure, human rights, employment and industrial relations, environment, bribery and corruption, consumer interests, science and technology, competition, and taxation. Their purpose is to ensure that business operations are in harmony with government policies, to strengthen the basis of mutual confidence between businesses and the societies in which they operate, to improve foreign investment climate, and to enhance the contribution of the private sector to sustainable development. The *Guidelines*, together with the UN *Guiding Principles* and the fundamental ILO Conventions, are one of the major international instruments on RBC.

A precise definition of a multinational enterprise (MNE) is not required for the purpose of the *Guidelines*. These enterprises operate in all sectors of the economy; their ownership may be private, state or mixed; and they comprise all entities within the enterprise, i.e. parent companies and local entities. The *Guidelines* do not aim to introduce differences of treatment between multinational and domestic enterprises – they reflect good practice for all. Adherents wish to encourage the widest possible observance of the *Guidelines* to the fullest extent possible, including among small- and medium-sized enterprises even while acknowledging that these businesses may not have the same capacities as larger enterprises.

Adherents to the *Declaration* use the *Guidelines* for several policy purposes, at both national and international level. The *Guidelines* provide comprehensive and clear guidance on the expected behaviour of businesses operating in or from jurisdictions of adherents; help protect public interest and stakeholder rights; and promote a more open, transparent, and better business and investment climate. Because of their breadth and scope, the *Guidelines* can also be useful for framing and strengthening the links between policy areas that govern business conduct, such as, for example, corporate governance and risk management for environmental and social issues. Therefore, the *Guidelines* can be used to promote policy coherence and a whole-of-government approach to policies that concern business behaviour.

Furthermore, the *Guidelines* also contribute to improved accountability in case of issues that can arise from their non-observance. Setting up an NCP is an obligation of each country that adheres. NCPs have a mandate to further the effectiveness of the *Guidelines* by undertaking promotional activities, handling inquiries, and contributing to the resolution of issues that arise if the *Guidelines* are not observed by businesses in specific instances. NCPs provide one of the few government-based, non-judicial grievance mechanisms with such an effective and broad application. NCPs offer, and with the agreement of the parties involved, facilitate access to consensual and non-adversarial means, such as conciliation or mediation, to resolve issues that arise if the *Guidelines* are not observed. This problem solving focus of NCPs allows the involved parties to exercise a better level of control over the process of reaching an agreement than more formal processes in which a third unrelated party makes a final binding decision. This can often be a significantly more expeditious and cost saving alternative to more formal procedures, and, in cases where there are no reliable procedures available, can often be the only venue available.

NCPs also have an important promotion and stakeholder engagement function. They are expected to develop and maintain relations with representatives of the business community, worker organisations and other interested parties that are able to contribute to the effective functioning of the *Guidelines*. NCPs are expected to make the *Guidelines* known and available by appropriate means, to raise awareness about them and their implementation procedures, including also with prospective investors (outward and inward).

Furthermore, Adherents have also agreed to help businesses, through a multi-stakeholder process and in co-operation with the NCPs, identify and respond to risks of adverse impacts associated with particular products, regions, sectors or industries. Guidance on due diligence has been developed for the extractives and agricultural supply chains (see Box 7.4) and is currently being developed for the garment and footwear and financial sectors.

Box 7.4. **How responsible agricultural supply chains can contribute to sustainable development**

Investing in agriculture is one of the most effective strategies for economic growth and poverty reduction in rural areas. GDP growth originating in agriculture is at least twice as effective in reducing poverty as GDP growth originating outside agriculture (World Bank, 2008). However, agri-business investments can also have adverse social and environmental impacts, particularly in countries with weak governance frameworks. Conflicts between investors and affected stakeholders can lead to social polarisation and political instability, and translate into reputational, operational and, thus, financial risks for investors. For instance, if land tenure rights are not well defined and protected, small land tenure rights holders may enter into unfair contracts with large agri-business investors that have higher bargaining power.

Businesses have a key role to play in ensuring that their operations do not have adverse impacts and benefit local communities and host countries. Their observance of responsible business conduct standards, as outlined in the 2016 OECD-FAO Guidance for Responsible Agricultural Supply Chains that aims to aid the implementation of the *Guidelines for Multinational Enterprises* can ensure that they contribute to sustainable development. The guidance calls on companies to:

- Ensure that their operations contribute to food security and nutrition and sustainable and inclusive rural development;
- Continuously assess and address the actual and potential impacts of their operations, processes, goods and services over their full life-cycle;
- Disclose timely and accurate information related to risk factors and their responses to particular environmental, social and human rights impacts;
- Respect human rights and core labour standards and strive to increase employment opportunities;
- Establish and maintain an appropriate environmental and social management system and continuously improve their environmental performance; and
- Prevent and abstain from any form of corruption and fraudulent practices.

Kazakhstan's National Contact Point

Upon adherence to the OECD Declaration, Kazakhstan plans to establish the NCP in the Investment Committee of the Ministry for Investments and Development (MID) and to form a multi-stakeholder Working Party to assist it in its functioning. The Committee is the authorised state body responsible for implementation of the *Guidelines* and the establishment of the NCP according to Decree No. 1452 (16 November 2012). MID has led Kazakhstan's process of

adherence and is fully aware of the extent of commitments Kazakhstan will have to implement as a result of adherence, including as related to the *Guidelines* and the NCP. The OECD and MID organised a joint conference on 29 June 2016, chaired by the Vice Minister, to share information with the Kazakh authorities and relevant stakeholders about RBC, the *Guidelines*, and the NCP mandate, structure, and core criteria, as well as how NCPs resolve issues in practice. Around 50 participants attended the workshop, representing different parts of MID, but also Ministries of Foreign Affairs, National Economy, Energy, Finance, as well as representative of all stakeholder groups. Representatives of MID and the Ministry of National Economy also attended the 2016 Global Forum on Responsible Business Conduct and the Meeting of the National Contact Points on 7-10 June 2016.

In the government's view, the Investment Committee and MID's combined experience, breath of responsibilities, and available resources, in addition to the establishment of the Working Party, create the most appropriate conditions in the national context of Kazakhstan for establishing a robust, transparent and easily accessible NCP that is capable of fulfilling all of its functions effectively. The government has defined key NCP functions in line with the objectives set out in the *Guidelines,* namely raising awareness, including through seminars and other promotion and dissemination activities; providing advice and explanation about the NCP mandate; processing specific instances and co-operating with other NCPs as necessary in consideration of specific instances.

The NCP will be staffed by 5 part-time experts from the Investment Policy Division under the Investment Committee, who will act as a Steering Committee and whose range of responsibilities will include arranging Working Party meetings, disseminating information, organising seminars and awareness-raising events, maintaining the NCP website, drafting the NCP annual report, receiving complaints under the specific instance procedures and disseminating them to the Working Party for further processing. The NCP will report to the Working Party. The NCP budget will be provided under the general budget of the Investment Committee.

A draft action plan for NCP activities is being elaborated and is expected to be approved in January 2017. The government has reported that the planned actions include workshops to promote the *Guidelines*, promotion of RBC activities, notification of diplomatic missions about the establishment of the NCP and its services, development of recommendations for the preparation and publication of the annual report on NCP activities; activities to strengthen the implementation of international standards for protecting women's rights; organisation of meetings of the Republican Tripartite Commission on Social Partnership and Regulation of Social and Labour Relations (see section below) at the national, sectoral and regional levels on issues related to labour rights;

organisation of meetings on combating corruption; activities to incentivise RBC by companies such as awards or contests for best practices.

The multi-stakeholder Working Party will act both as an advisory and oversight board and will be the main decision-maker as related to specific instances. It will be headed by the Chair of the Investment Committee of the Ministry for Investments and Development. The list of Working Party members was approved through Decree No. 95 of the Chairman of the Investment Committee of the Ministry for Investments and Development on 22 November 2016. It includes a list of around 30 members, with representation from the Ministry of Healthcare and Social Development, Ministry of Energy, Ministry of Agriculture, Ministry of Internal Affairs, Ministry of Education and Science, Ministry of Foreign Affairs, Agency for Civil Service Affairs, the National Chamber of Entrepreneurs and several joint stock companies, National Center for Human Rights, and Legal Policy Research Centre. The list is open for extension and any organisation may apply for inclusion through a formal request (official letter). In the view of the government, the inclusion of different stakeholders in the Working Party is meant to fight conflicts of interest and ensure that the NCP operates in an impartial manner while maintaining an adequate level of accountability to the government and in accordance with core criteria of visibility, accessibility, transparency and accountability. Additionally, including stakeholders outside of the government is meant to ensure that the NCP retains the confidence of social partners and other stakeholders, and fosters the public profile of the Guidelines as envisioned in the Guidelines. The Working Party will meet at least on a quarterly basis or as needed for specific instances.

Rules of procedures for accepting specific instances as well as the distribution of responsibilities between the NCP and the Working Party for specific instances will be approved at the first meeting of the Working Party in January 2017. Envisioned procedures for handling specific instances involve formal notification to the Working Party by the Investment Committee, requesting positions of the Working Party members, and a subsequent meeting during which the Working Party will examine it and make decisions by consensus.

The Investment Committee and the NCP by extension are expected to maintain a dialogue with stakeholders on a regular basis. The information on the activities of the NCP, as well as contacts of the Committee representatives responsible for the implementation of NCP activities will be published on the MID website and on Kaznex Invest website. The Committee is also expected to carry out an annual seminar to promote the *Guidelines* with all stakeholder groups.

Alleged RBC issues in Kazakhstan have already been considered by the National Contact Points under the *Guidelines*. In July 2013, the UK, US and Italian

NCPs received a request for review from NGOs alleging that KPO Consortium had breached the general policies, and human rights provisions of the *Guidelines* in Kazakhstan. The request covered a period from the early 2000s to the present, and the allegations made relate to obligations to resettle villagers in view of emissions levels and other environmental impacts of relevant facilities. Taking into account the facts of the request, the situation of the parties and the capacity of NCPs to provide good offices should the issues merit this, the NCPs decided that the UK NCP should act as lead NCP while the US and Italian NCPs would provide support. The UK NCP conducted an initial assessment and concluded that the specific instance merits further examination with respect to the limited issue of individual households legally entitled to resettlement. The details of the NCP decision and next steps are outlined in an initial assessment issued in November 2013.[24] The specific instance is currently ongoing.

General policies for promoting responsible business conduct in Kazakhstan

In line with global trends, RBC has emerged as an important topic in Kazakhstan. As summarised in the 2014 OECD *Responsible Business Conduct in Kazakhstan* report (2014 RBC report), numerous RBC-related public and private initiatives have been established since the first National Forum on Corporate Social Responsibility in 2008 and the launch of the Paryz awards to recognise leading enterprises in the field and provide incentives for integrating responsibility into decision-making processes. Notable efforts between 2008 and 2014 include the elaboration of a CSR policy by Samruk-Kazyna, Kazakhstan's sovereign wealth fund and joint stock company, and the ongoing promotional activities by the National Chamber of Entrepreneurs and civil society organisations such as the Legal Policy Research Centre and Eurasia Foundation of Central Asia (OECD, 2014a).

A number of promising developments have emerged since 2014. In April 2015, a draft CSR concept was adopted at a meeting of the Republican Tripartite Commission on Social Partnership and Regulation of Social and Labour Relations, chaired by the Prime Minister. The concept was introduced by the National Chamber of Entrepreneurs (NCE) on the basis of a draft outline developed by the Eurasia Foundation of Central Asia (LPRC, 2016; Government RK, 2015a; Atameken, 2015). The concept includes a reference to the *Guidelines*. The government has reported that the Tripartite Commission approved a plan in July 2016 to promote the CSR concept for 2016-17. The NCE is also piloting sectoral agreements in order to promote social dialogue. For example, in May 2016, a two year programme was launched with energy companies to promote better industrial relations and development of human capital (Atameken, 2016a). The government has reported that several activities have also been

undertaken by regional chambers of entrepreneurs, for example seminars in the Almaty, Pavlodar, Aktobe and South Kazakhstan regions in October-November 2015 on political activities and the responsibilities associated with undertaking such activities. Furthermore, the government has reported that industry associations are planning to undertake an industry-wide effort to promote CSR such as the 2012-13 effort by KazEnergy to review *Social Responsibility in the Oil and Gas Sector of the Republic of Kazakhstan* (KazEnergy, 2016). There have also been notable efforts by Samruk-Kazyna to improve corporate governance as already noted in Chapter 2 of the present *Review*.

On a policy level, a new Entrepreneurial Code, which superseded the Law on Private Entrepreneurship among others, was enacted in early 2016. The legal definition of RBC had been given in the Law on Private Entrepreneurship (art. 1.2) as "social responsibility of business – voluntary contribution of private business entities in development of the society in the social, economic and ecological spheres" and has largely been kept. However, the new code expands on the concept in a new *Chapter on Social Responsibility of Business*. The voluntary nature of social responsibilities is underlined throughout the text, with charity (with tax benefits) mentioned as one form through which businesses can undertake social responsibility. Two prioritised thematic areas are featured – employment and labour relations and the environment.

Notably, the state itself also commits to create conditions for social responsibility and separates the functions of state and businesses, underlining that the state should not interfere with businesses in the exercise of charity. These are welcome developments, particularly in light of the previous reports that the contributions of enterprises under the previous Law on Private Entrepreneurship were rarely voluntary in practice and investors often perceived them to be charity tax, with limited input in the selection and implementation of projects (OECD, 2014a). Particular attention needs to be paid to ensure the implementation of these provisions. It should be also noted that, while charity is a legitimate form for businesses to engage with the society, RBC is considered to more comprehensive than philanthropy and focuses on integrating environmental and social considerations into core business operations.

These developments point to an increasing, although not yet widespread, awareness of the importance of RBC in Kazakhstan. Efforts should be made to ensure that existing initiatives are sustained. For example, some promising initiatives discussed in the 2014 RBC Report seem to have stopped. When the Ministry of Labour and Social Protection of Population (whose mandate has now been enveloped into the Ministry of Healthcare and Social Development) launched the agreements to promote UN Global Compact Principles with relevant stakeholders, including the National Chamber of

Entrepreneurs, more than 226 enterprises were signatories. As of June 2016, only 5 companies were listed as active (UN Global Compact, 2016).

Stakeholders have continuously called for co-ordinated action by the government on RBC in order to address some of these gaps.[1] The government has yet to develop a comprehensive RBC policy or strategy as recommended by the 2012 *Investment Policy Review*. Although several Ministries have implemented initiatives related to RBC, it has been on an *ad hoc* basis and they remain fragmented (OECD, 2014a). Though the government reports that a focal point on RBC was established in MID in 2012, it does not appear to be functional in practice. Kazakhstan's adherence to the OECD *Declaration*, and, in particular, the formal establishment of an NCP under the *Guidelines*, will be an opportunity to consolidate efforts by the stakeholders and further promote RBC principles and standards, both within the government and with the wider public and to clarify and set out the government's exact expectations on RBC.

The government should consider working with stakeholders to develop a National Action Plan (NAP) on RBC, in line with international good practice and based on the *Guidelines*. The UN has strongly encouraged all states to develop a NAP on Business and Human Rights as part of the state responsibility to disseminate and implement the UN *Guiding Principles*. A number of OECD governments, notably the United States, have decided to broaden these efforts and include RBC issues, based on the *Guidelines*, in their NAPs. Considering the alignment between the UN *Guiding Principles* and the *Guidelines*, this approach is complementary with UN recommendations and efforts. The UN Working Group on Business and Human Rights has set up a dedicated webpage on NAPs to provide easy access to existing plans, as well as key public information and analysis on the various stages of NAP development, implementation and follow up (UN OHCHR, 2016a).

The process of developing a NAP would be a good way for the government to engage with stakeholders and the wider public on a range of issues related to RBC, to promote the *Guidelines*, as well as policy coherence and alignment on RBC. The NCP, in coordination with relevant government and other stakeholders, could lead the process. The process of developing the NAP would also be a good way for the government to understand and eventually remove barriers that influence RBC uptake by businesses, as well as to facilitate collective initiatives to promote RBC among industry and other stakeholders. The process of developing an NAP could also serve to assess barriers to ensuring the implementation of Pillars I and III of the UN *Guiding Principles* - the State Duty to Protect Human Rights and Access to Remedy respectively - in the context of Pillar II, the Corporate Responsibility to Respect Human Rights. These two pillars focus on preventative and remedial measures as related to the role of governments and should not be overlooked.

Leading by example – RBC and the activities of state owned enterprises

Governments are expected to lead by example on RBC, including in their own practices, i.e. as employers, business partners, through procurement and contracting practices, and in commercial activities, including activities of state-owned enterprises (SOEs). As already mentioned in the previous section, the *Guidelines* apply to all entities within the enterprise in all sectors, whether of private, state or mixed ownership. The same is true for the UN *Guiding Principles*, which apply to all states and all enterprises. UN *Guiding Principle* 4 stipulates that states "should take additional steps to protect against human rights abuses by business enterprises that are owned or controlled by the State, or that receive substantial support and services from State agencies such as export credit agencies and official investment insurance or guarantee agencies, including, where appropriate, by requiring human rights due diligence" (UN, 2011). The UN Working Group on Business and Human Rights recently examined RBC practices of SOEs and found that there is a general lack of attention to RBC issues and has called on states to explicitly fill these gaps (UN, 2016).

The importance of RBC in SOE activities has been recognised beyond the *Guidelines* and the UN *Guiding Principles*. The 2015 OECD *Guidelines on Corporate Governance of State-Owned Enterprises* (*SOE Guidelines*) recommend that the state ownership policy fully recognise SOE responsibilities towards stakeholders and request that SOEs report on their relations with stakeholders, as well as to make clear any expectations the state has in respect of RBC by SOEs (OECD, 2015e: V). The *SOE Guidelines* further recommend extensive measures to report on foreseeable risks, including in the areas human rights, labour, the environment, and risks related to corruption and taxation.

As mentioned earlier in this report, considering that public and state-owned companies account for a large share of GDP, totalling more than 7 000 companies, they have significant leverage and can improve the quality of the business environment. In addition to having set out a CSR policy, Samruk-Kazyna has recently taken important steps to improve its corporate governance framework. A new Corporate Governance Code was adopted in 2015 and applies to all organisations in which the fund owns more than 50% of voting rights. The code calls for transparency and accountability of internal audit systems, comprehensive and systemic risk management, observance of human rights, prevention of environmental abuse, intolerance of corruption and other integrity related aspects. It also requires disclosure of these issues in the annual reports of the fund and its subsidiaries (OECD, 2016). The Code sets out that the fund and its organisations should develop action plans on sustainable development, with the *Guidelines* mentioned as a relevant international standard (Samruk-Kazyna, 2015). The government has reported that the Code is currently being introduced in Samruk-Kazyna affiliated companies. First

compliance reports are expected in 2017. Additionally, a specific hotline number and a confidential email to report any alleged violations has been established.

The government should establish expectations on RBC and should publicly disclose these expectations, as well as establish mechanisms for their implementation. More broadly, this is true in general for corporate governance beyond SOEs. RBC and corporate governance are intrinsically linked as, on the one hand, RBC impacts the company's decision-making processes, risk management, disclosure and transparency, and relationships with investors and stakeholders; and, on the other hand, the actual process of undertaking due diligence is closely related to the corporate governance framework and the relationships between company management, board, shareholders and other stakeholders. The *G20/OECD Principles of Corporate Governance* reflect the expectations set out in the *Guidelines*, including the expectation that the corporate governance framework recognises the rights of stakeholders and encourages active co-operation with them; ensures timely and accurate disclosure on all material matters regarding the corporation; and reflects high ethical standards (G20/OECD, 2015). The government should ensure, as a matter of policy coherence, that corporate governance reforms adequately address, describe and reflect the extent of corporate responsibilities related to environmental and social matters.

Policies in specific areas covered by the OECD Guidelines

In addition to general recommendations on RBC, the *Guidelines* include specific recommendations to enterprises in the areas of information disclosure, human rights, employment and industrial relations, environment, bribery and corruption, consumer interests, science and technology, competition, and taxation.

Disclosure

Disclosure is an integral part of RBC and corporate governance. Clear and complete corporate information is important to a variety of users, from shareholders to workers, local communities, governments and the society at large. The *Guidelines* call for timely and accurate disclosure on all material matters regarding the corporation, including the financial situation, performance, ownership and governance of the company. The *Guidelines* also encourage disclosure in areas where reporting standards are still evolving such as, for example, social, environmental and risk reporting. These expectations align with the expectations set out in the *G20/OECD Principles of Corporate Governance*. Many businesses already provide information on a broader set of topics than financial performance and consider disclosure of non-financial information a method by which they can demonstrate a commitment to

socially acceptable practices. Additionally, the process of gathering and thinking through data pieces needed for effective non-financial disclosure is not only relevant for communication and reporting, but also serves as invaluable input for strategic planning, decision-making, and risk management.

Corporate governance requirements, including on disclosure and reporting, are still evolving in Kazakhstan. Out of 140 examined economies in the World Economic Forum (WEF) 2015/2016 Global Competitiveness Index, Kazakhstan ranks lower in areas related to corporate governance than average among the 46 adherents to the OECD *Declaration*: for example, strength of auditing and reporting standards (74 vs average of 44), efficacy of corporate boards (58 vs average of 50), and protection of minority shareholders' interests (52 vs average of 50). The rankings are based on the WEF's executive opinion survey and the World Bank's *Doing Business* indicators.

The Joint Stock Company Law and Law on Accounting and Financial Reports are the legal basis for corporate disclosure in Kazakhstan (OECD, 2014a). Kazakhstan also adopted a voluntary corporate governance code in 2005, approved by the Council of Issuers of the Kazakhstan Stock Exchange, and amended in 2007, although a recent OECD review has pointed out that the code does not fully align with OECD standards of corporate governance and that practical implementation remains weak (OECD, forthcoming). Disclosure of non-financial information, such as social and environmental performance, is weak and remains on a voluntary basis. Disclosure requirements for enterprises to include environmental and other non-financial performance have partially been expanded, as recommended by the 2012 *Investment Policy Review*. The inclusion of a specific chapter on Transparency in the 2015 Corporate Governance Code of Samruk-Kazyna and the disclosure requirements as referenced in the above section are welcome developments. Additionally, the July 2016 plan of the Tripartite Commission to promote the CSR concept for 2016-2017 also includes specific activities geared at promoting non-financial disclosure. The government has reported that the Ministry of National Economy has approved a model corporate governance code in accordance with OECD principles and standards on 1 November 2016 by the Decree No. 465 of the Minister of National Economy.

Some promising initiatives have recently emerged. Since September 2015, Kazakhstan Stock Exchange (KASE) participates in the Sustainable Stock Exchanges Initiative (SSEI) and has committed to promoting long-term sustainable investment and improved environmental, social and corporate governance disclosure and performance among its companies (SSEI, 2015). A 2015 study showed that there has been some progress in non-financial disclosure of the top 20 Kazakh companies by market capitalisation – 47% have published some form of non-financial information or integrated reports on their website, as compared to 40% in 2012 (Novikova, 2015).

Due to the importance of the extractives sector, sector-specific initiatives have also been implemented. In October 2013, Kazakhstan was declared compliant with the Extractive Industries Transparency Initiative (EITI), which aims to promote revenue transparency in the oil and gas industry. This was the culmination of a process that began in 2005 when the government, businesses (foreign and domestic) and civil society signed a Memorandum of Understanding that committed the parties to implement the EITI. This commitment was promoted in the 2010 Law on Subsoil and Subsoil Use (art. 76) that required all companies to comply with the terms of the MoU and to confirm compliance through an audit report. A new MoU requiring the parties to implement the EITI was signed on 9 October 2013. As mentioned in Chapter 3, the government is currently preparing a new subsoil code. The EITI requirements have remained as of the February 2016 draft. The EITI implementation is supervised by a National Stakeholders' Council, which is a multi-stakeholder body. The National Stakeholder Council is currently undertaking a review process to identify new activities for EITI implementation, in light of the deadline for the next EITI report at the end of 2016. The EITI website reports that there seems to be considerable interest among stakeholders to decentralise the EITI process and establish regional multi-stakeholder forums, in particular in resource-rich provinces (EITI, 2016).

More efforts should be made to encourage companies to be more transparent in general, but also to disclose information on non-financial issues. This could be done by promoting disclosure of information based on the *Guidelines* disclosure chapter, or through supporting dedicated campaigns and targeted programs, including support for multi-stakeholder initiatives, such as the Global Reporting Initiative or the Integrated Reporting Framework. The government has a leading role to play in these efforts, particularly in terms of clarifying the requirements in this area.

Experience from Adherents to the Declaration is of relevance in this area. In 2014, the EU issued a Directive (2014/95/EU) for the European Economic Area on disclosure of non-financial and diversity information, amending the 2013 Accounting Directive (2013/34/EU). The new Directive requires companies of a certain size to disclose in their management reports information on policies, risks and outcomes related to environmental matters, social and employee aspects, respect for human rights, anticorruption and bribery issues, and diversity in their board of directors, aiming to provide investors and other stakeholders with a more comprehensive picture of company performance (EU, 2014). Article 9 of the Directive states that business could rely on the *Guidelines* framework to meet these requirements. Kazakhstan should consider adopting a similar measure in order to approach international standards in the area of corporate governance, as well as a way of encouraging non-financial disclosure with the business community and promoting the *Guidelines*. Other examples of

strengthened disclosure requirements include Section 1502 of the 2010 United States Dodd–Frank Wall Street Reform and Consumer Protection Act for minerals supply chains, which directs certain companies to undertake efforts to ascertain the origin of tin, tantalum, tungsten and gold in their mineral supply chains. If the minerals are considered to come from the Democratic Republic of Congo or adjoining countries, or if the mineral provenance is unknown, then the issuers are required to undertake due diligence and file additional disclosures about the minerals.[2] Additionally, in March 2015, the UK enacted the Modern Slavery Act, mandating that commercial organisations prepare an annual statement on slavery and human trafficking and report on their due diligence processes to manage these risks within their operations and supply chains (UK, 2015).

Human rights

As recognised by the *Guidelines* and the UN *Guiding Principles*, states have a primary duty to protect human rights. However, businesses are expected to respect human rights independently of the state ability and willingness to fulfil its human rights obligations. Failure either to enforce relevant domestic laws or to implement international human rights obligations, or the fact that the state may act contrary to those laws and obligations, does not diminish obligation of businesses to respect human rights (OECD, 2011; UN, 2011).

Kazakhstan has ratified 8 of 9 core international human rights instruments[3] (UN OHCHR, 2016b, d). Kazakhstan has also ratified 24 ILO Conventions, including the eight fundamental Conventions and four priority Governance Conventions (ILO, 2016a).[4]

Human rights are recognised and guaranteed in Kazakhstan's Constitution (article 12) by virtue of birth and are recognised to be absolute and inalienable (Government RK, 2007). The reforms in the *2050 Strategy* are also based on protecting and upholding human rights through modernising the state and society, in part by strengthening the rule of law, state accountability and transparency. The protection of human rights and freedoms is cited as one the main objectives of the *Foreign Policy Concept* developed on the basis of the *2050 Strategy* (Government RK, 2014a). A Commission on Human Rights has been established as a consultative and advisory body under the President (e-gov, 2016). A formal National Human Rights Ombudsman (sometimes also often referred as the Human Rights Commissioner) has also been established and has a mandate to address complaints related to human rights abuses. The Ombudsman is appointed by the President (Ombudsman, 2016).

To date, one of most ambitious government efforts to bring about improvements in protecting human rights in Kazakhstan has been the adoption of a National Human Rights Action Plan for 2009-2012. Developed through a

multi-stakeholder process, on the basis of the results of the Baseline Report on Human Rights in Kazakhstan, the Plan intended to consolidate the steps for improving human rights legislation and the national system of protection of human rights, and to promote education on human rights and the mechanisms for their protection (UNDP, 2009). However, independent experts have stated that only 23% of the recommendations were implemented and human rights defenders have noted that the recommendations did not address some of the main human rights issues, in either the legislation or in law-enforcement practices (EU, 2013). The findings in the 2014 report on the activities of the Ombudsman also support the observations that the human rights situation in Kazakhstan needs to be improved - remediation was found for only 13.8% of the 716 complaints accepted for consideration by the Ombudsman (out of 1330 total received complaints) (Ombudsman, 2015).[5] In 2014, the Kazakhstan International Bureau for Human Rights and Compliance with Laws, the Legal Policy Research Centre, and MediaNet, with the support of the EU, submitted a Concept for the next National Plan of Action for Human Rights for 2015-20.[6] The plan, however, has not yet been developed or adopted.

Concerns about the human rights situation in Kazakhstan, also as connected to business activities, have been raised by international organisations, some OECD member governments, and human rights defenders. Business and human rights issues in Kazakhstan drew particular attention following the 2011 Zhanaozen crisis when clashes between demonstrators and police resulted in deaths and casualties.[7] Although the government has made efforts to investigate and prosecute responsible parties, the UN Special Rapporteur on the Rights to Freedom of Peaceful Assembly and of Association noted after a country visit in 2015 that there is still conflicting information on what happened in Zhanaozen and has joined the Office of the High Commissioner for Human Rights call for an independent international investigation into the crisis (UN, 2015a). The UN Special Rapporteur has also raised concerns that, since Zhanaozen, participants in unsanctioned assemblies seem to have been increasingly subjected to intimidation, fines, imprisonment and administrative sanctions.

Additionally, the UN Special Rapporteur, the United States, the European Union and civil society have expressed concerns that the new Criminal Code, Code on Administrative Offences and Code of Criminal Procedure adopted in 2015 could negatively affect or limit fundamental freedoms, including the right to freedom of association[8] and that provisions in the codes could be used to criminalise the activities of political parties and trade unions (UN, 2015a). Kazakhstan has refuted this criticism and has stated that the codes are in line with international standards on preservation of interethnic harmony and stability and that the practice of applying these provisions should not raise questions (UN, 2015b). A review Kazakhstan's implementation of the

International Covenant on Civil and Political Rights (ICCPR) took place on 22-23 June in Geneva (UN OHCHR, 2016d). While the final Committee report is not available as of the date of this draft report, it should be noted that a collection of Kazakh Human Rights NGOs, including the above mentioned which gave advice to the government on the 2015-2020 National Action Plan on Human Rights, have expressed serious concerns about the deteriorating human rights situation in Kazakhstan (IPHR, 2016 a-b).[9] The recent protests over land reform and the related arrests, detention and criminal prosecutions point to the fact that some of these concerns are not unwarranted. UN human rights experts have called on the government to "immediately end all forms of persecution and take effective measures to protect civil society" (UN OHCHR, 2016c). Protesters were concerned that amendments to the land law increasing lease terms for foreigners for renting agricultural land from 10 to 25 years would be to the detriment of Kazakh citizens and landowners (BBC, 2016; Al Jazeera, 2016; APF, 2016). The intensity of the protests has led to delaying the adoption of the amendment by a year (APF, 2016).

It is unclear how much of these protests are over the actual substance of the proposed amendments and how much are a reaction to the perceived corruption, distrust, and the historical legacy of privatisation (BBC, 2016). As already stated in this review, the current 10 year maximum rental time by foreigners is relatively restrictive compared to OECD economies (OECD, 2012) and may be holding down the country's potential in agricultural production (OECD, 2013). However, fears around liberalisation should be addressed. Establishing a strong NCP and explicitly stating and implementing expectations on RBC in line with the *Guidelines* and the *UN Guiding Principles* may help alleviate some of the concerns around investment and help build trust. The development of the NAP on RBC could be a good opportunity for the government to engage with stakeholders. Kazakhstan should also consider revisiting some of the provisions that the international stakeholders have raised concerns about.

Employment and industrial relations

Kazakhstan's labour market is characterised by the population of a working age (15 to 64 years old) accounting for 67% of total population (UN DESA, 2015), with labour force participation rate at 73% in 2014, comparable to other emerging economies (ILO, 2014). Agriculture is both the least productive sector and the largest employer, accounting for around 24% of employment in 2013. The 2016 OECD *Multi-dimensional Review of Kazakhstan* noted that there is a need to shift labour to more productive sectors in order to address productivity concerns. There is potential to broaden the industrial base from a relatively low GDP share of manufacturing at 11% compared to other emerging economies as well as advanced, resource-rich countries (OECD, 2016). Job

quality remains an issue for a large number of workers concentrated in several sectors and regions and concerns about low wages, non-payment of wages and discrimination have been raised by stakeholders when it comes to foreign investors (OECD, 2014).

The 2015-16 WEF *Global Competitiveness* report has indicated that inadequately educated workforce is among the most problematic factors for doing business in Kazakhstan. Finding qualified staff, good quality local products and suppliers remains difficult, especially for technical personnel and in rural areas. As Kazakhstan phases out local content requirements as part of its WTO obligations, this *Review* notes (see Chapter 5) that the planned development of the database of local suppliers and MNEs operating in different sectors by Kaznex Invest could help local and foreign enterprises learn about the locally available opportunities. Chapter 5 recommends that these activities be complemented with active matchmaking events and that IPA, MID or other government agencies can facilitate the creation of specific capacity-building programmes for local firms and develop and implement them in close collaboration with investors.

Suppliers of MNEs may find that following RBC principles and standards and integrating them in core business operations gives them an advantage over businesses that do not, as they are able to respond to and address concerns that may come up in due diligence of the MNE when evaluating risks associated with its supply chain. Investors from the 46 countries that adhere to the *Guidelines* are subject to them wherever they operate, including throughout the supply chain and in relation to business relationships. Similarly, businesses that want to access markets of these 46 countries are also subject to the *Guidelines*, and, in some cases, actual regulation related to RBC. Additionally, MNEs are increasingly basing their decisions about where to do business on the ability to ensure predictable and reliable supply chains, capable of delivering effectively at the each stage (Taglioni and Winkler, 2014; OECD, 2014b: 27). It is estimated that costs of delays can be substantial for certain product categories and any delays due to, for example, labour unrests or environmental damage, contributes to those costs. (Hummels, 2007; OECD, 2014b: 27).

Building on the recommendations from Chapter 5, the government should consider including RBC principles and standards in the design of the systematic and well-institutionalised industry-specific training programmes, in collaboration with the business community and educational institutions. This could encompass everything from promotion to capacity building exercises to supporting cross-sectoral learning efforts (for example, supporting cost-sharing efforts within and among industries for specific due diligence tasks, participation in initiatives on responsible supply chain management and co-operation between industry members who share suppliers).

RBC expectations should also be included in FDI attraction efforts and may help attract MNEs that are more inclined to source locally. One element of supplier databases and matchmaking events could be RBC. Additionally, training and awareness-raising with business leaders could also be useful in promoting a wider understanding and recognition of the importance of RBC. Educational institutions such as business schools and existing business initiatives pursing social objectives can also be important platforms. Finally, the authorities should make educational and training programmes more market driven by increasingly involving the private sector in human resource development policies and encouraging internal and external training by employers.[10] Communicating to enterprises that contributing to human capital formation (in particular by creating employment opportunities and facilitating training opportunities for employees) is a pillar of RBC – and recognising those that do it – can serve as a good incentive.

There is also a need to bring about full alignment of Kazakhstan's legal framework on labour relations with international standards. Although Kazakhstan has ratified 24 ILO conventions, including the eight Fundamental Conventions and four Governance Conventions (ILO, 2016), serious concerns have been raised about limited freedoms in practice, as noted in the above section on Human Rights. The ILO Committee on the Application of Standards at its recent meeting in June 2016 has also "expressed serious concern regarding the Government's lack of progress in relation to the implementation of the conclusions of the Committee in 2015" and urged the government to introduce reforms in the legal framework governing labour relations without delay. Specifically, the committee recommended to amend the 2014 Trade Union Law, including as related to limitations on the structure of trade unions that are perceived to limit the right of workers to form and join trade unions of their own choosing; to amend the provisions of the Law on the National Chamber of Entrepreneurs to ensure the full autonomy and independence of the free and independent employers' organisations; to amend the Labour Code to indicate which organisations fall into the category of organisations carrying out dangerous industrial activities and indicate all other categories of workers whose rights may be restricted, to ensure any minimum service is a genuinely and exclusively minimum; to permit judges, firefighters and prison staff to form and join trade unions; to lift the ban on financial assistance to national trade unions by an international organisation; and to accept ILO technical assistance to complete the above noted conclusions (ILO, 2016b). Concerns about the existence of forced and child labour in Kazakhstan has also been expressed in recent years.[11] A new Labour Code entered into force as of January 2016. In the government's view, the code is fully aligned with OECD and ILO standards (Government RK, 2016). Reactions by stakeholders have been mixed. Workers'

rights advocates have expressed concerns about the lack of public consultation and debate prior to the adoption of the code (Eurasianet, 2015).

Kazakhstan could consider making a particular effort to promote the good offices envisioned as part of the mandate of the NCP for the *Guidelines* as one of the available non-judicial mechanisms for resolving issues related to employment and labour relations. The *Guidelines* are a useful framework for determining the extent of enterprise responsibilities in this regard. This is not only related to respecting fundamental labour rights, but also includes principles of equality of opportunity and treatment in employment and non-discrimination; provision of best possible wages, benefits and conditions of work; as well as provision of training with a view to improving skill levels, in co-operation with worker representatives and, where appropriate, relevant governmental authorities.

Environment

The *Guidelines* call on enterprises to take due account of the need to protect the environment, public health and safety, and generally to conduct their activities in a manner contributing to the wider goal of sustainable development. This entails sound environmental management that aims to control both direct and indirect environmental impacts; establishing and maintaining appropriate environmental management systems; improving environmental performance; being transparent about the environmental impacts and risks, including also reporting and communicating with outside stakeholders; being proactive in avoiding environmental damage; working to improve the level of environmental performance in all parts of their operations, even where this may not be formally required; and training and education of their employees with regard to environmental matters.

Kazakhstan ranks 69 out of 180 in the 2016 Yale Environmental Performance Index, with an assessed 25% positive change in environmental performance compared to 10 years ago. Notable changes have been in improving water resources and air quality (Yale, 2016). The improvement in the ranking is a direct result of the efforts by the government over the last decade to modernise environmental legislation and address the legacies of the Soviet period. The main instrument for the protection of the environment is the 2007 Environmental Code. In May 2013, the Concept for Transition of the Republic of Kazakhstan to Green Economy was adopted, with the intention to invest 1% of GDP annually into green technologies. The 2050 Strategy sets forth an agenda which integrates environmental issues into economic policies; objectives include energy independence by 2025, water-saving measures for 15% of acreage by 2030, and addressing irrigation issues by 2040 (Government RK, 2015b). Kazakhstan is also a member of the OECD Task Force for the

Box 7.5. **Debunking the Pollution Haven Hypothesis**

2016 OECD report *Do environmental policies affect global value chains? A new perspective on the pollution haven hypothesis that* examined the impact of environmental policies on global value chains has shown that countries that implement stringent environmental policies do not lose export competitiveness when compared to countries with more moderate regulations. High and low pollution industries and trade in manufactured goods between 23 advanced and six emerging economies from 1990-2009 were examined, and data on the domestic value added in exports from the OECD-WTO Trade in Value Added (TiVA) dataset was included in the analysis.

The findings suggest that emerging economies with strong manufacturing sectors could strengthen and implement environmental laws without denting their overall share in export markets. High-pollution or energy-intensive industries would suffer a small disadvantage, but this would be compensated by growth in exports from less-polluting activities. These results are compelling evidence against the so-called Pollution Haven Hypothesis, which suggests that tightening environmental laws often prompts manufacturers to relocate some production stages to countries with lower regulations.

Source: Koźluk and Timiliotis, 2016.

Implementation of the Environmental Action Programme and is a signatory to the OECD Green Growth Declaration.

As outlined in the OECD *Multi-dimensional Review*, the country's reliance on fossil fuels weighs on the environment. The economy is characterised by high greenhouse gas emissions, reflecting the high energy intensity of the economy. Kazakhstan's fragile ecology is vulnerable to climate change and issues with water shortages and considerable pollution, even if improved compared to a decade ago, persist. Raising energy efficiency, developing renewable energy sources and improving the management of natural resources such as water, land and air, can improve the sustainability of the economy (OECD, 2016).

In practice, it has been reported that the administrative complexity and sometimes discretionary decision-making impedes the correct assessment of the true extent of possible environmental impacts of business activities. Some enterprises have complained about the lack of transparency of environmental regulations, and expressed concerns that the fines were imposed in an attempt to exert pressure and obtain additional funds (OECD, 2014a). Increasing the quality of institutions that are charged with environmental protection and promoting compliance with internationally recognised standards as a competitive opportunity that could open up opportunities for international trade are areas where better practice and co-ordination would bring benefits (OECD, 2016).

Finally, as discussed in the section on Disclosure, Kazakhstan should consider strengthening disclosure requirements and rules, including on environmental and climate change matters. Corporate climate change reporting is relevant for design and implementation of long-term actions aimed at reducing greenhouse gas emissions. A majority of G20 countries have some kind of mandatory corporate reporting scheme in place or in preparation that requires disclosure of some climate change related information. As new OECD research shows, this information can be used for multiple policy purposes, from informing consumer decisions to assessing performance against policy objectives, investment analysis and risk analysis. Companies themselves also use the information to increase awareness of climate related risks and opportunities, streamline processes, reduce costs and improve efficiency and mitigation or reversal of negative climate impacts (OECD, 2015b).

Combating bribery, bribe solicitation and extortion

As discussed earlier in this *Review* (see Chapter 5, Section on Addressing Business Concerns), bribery remains one of the main constraints for doing business in Kazakhstan, despite significant efforts made by the government to address the issue. The fight against corruption has become a national priority in the context of the *2050 Strategy*. Several measures have been implemented, including judicial and legislative reforms, and the establishment of dedicated bodies to fight bribery and other forms of unfair practices. Recent prosecution of high-level officials[12] also illustrate the willingness on part of the government to acknowledge the problem of bribery and to take practical measures to address it.

The *Guidelines* recognise the important role of the private sector in combating bribery and corruption. Enterprises should not, directly or indirectly, offer, promise, give, or demand a bribe or other undue advantage to obtain or retain business or other improper advantage, and should also resist the solicitation of bribes and extortion. As discussed in Chapter 5, recent steps have been taken by the authorities to encourage the development of preventive measures in the private sector through, for instance, the adoption of an Anti-Corruption Business Charter.

Consumer interests

Protection of consumer rights is codified in the Article 10 of the Civil Code of Kazakhstan and the Law on Protection of Consumer Rights. Consumers are granted the right to freely conclude contracts on the purchase of goods; access information on protection of consumer rights; access complete, reliable and timely information on a product and on the seller; purchase of safe products; free choice of a product; adequate quality of a product; exchange or return of a product of both adequate and inadequate quality; receipt of a seller's document confirming the fact of purchase of a product (LPRC, 2013). In May 2016,

amendments to a number of legislative acts related to consumer protection were passed, including on the Law on the Protection of Consumer Rights. New provisions were introduced to avoid unfair competition and to further protect consumers (Atameken, 2016b).

Overall, it appears that the legal framework is detailed and balanced enough to ensure protection of consumer rights. In practice, one of the main challenges encountered by consumers seems to be obtaining reliable information on a product (LPRC, 2013). The National League of Consumers, an NGO that is a member of Consumers International, provides independent information on goods and services, consumer education programmes, and ensures protection of consumer rights, including through a hot line dedicated to handle complaints and providing legal advice (Consumers International, 2016).

The *Guidelines* recommend that enterprises act in accordance with fair business, marketing and advertising practices and take all reasonable steps to ensure the quality and reliability of the goods and services that they provide when dealing with consumers. This includes co-operating fully with public authorities to prevent and combat deceptive marketing practices and to diminish or prevent serious threats to public health and safety or to the environment deriving from the consumption, use or disposal of their goods and services. It also includes supporting efforts to promote consumer education in order to improve the ability of consumers to make informed decisions, better understand the economic, environmental and social impact of those decisions, and support sustainable consumption.

Kazakhstan could consider supporting and promoting consumer education and information programmes in order to increase the capacity of civil society to be aware of consumer rights, to monitor government policy, and to promote effective defence of consumer rights. Particular efforts could be made to promote sustainable consumption. This may be an efficient strategy for reaching both economic and environmental objectives, as increased demand for sustainable products would lead to increased supply and investments into sustainable products. One area of particular interest for Kazakhstan could be organic agriculture in light of the increasing demand for organic products from European countries and from the United States (OECD, 2015c).

Science and technology

The chapter on science and technology of the *Guidelines* aims to promote, within the limits of economic feasibility, competitiveness concerns and other considerations, the diffusion by multinational enterprises of the fruits of research and development activities among the countries where they operate, contributing therefore to the innovative capacities of host countries. Intellectual property rights are of relevance in this regard.

Kazakhstan's ranks relatively low in international indexes on innovation considering its potential. According to the 2015/2016 WEF *Global Competitiveness* report, Kazakhstan ranks 72 out of 140 economies in overall innovation factors. Strategy 2050 emphasises the importance of investing in science and sets ambitious goals for developing a knowledge-based economy. The state programme of industrial-innovative development of Kazakhstan for 2015-2019, adopted by decree in 2014, notably aims to "increase the Global Competitiveness Index" and avoid the "middle-income trap" through measures focused on technology and innovation. The Program calls for the "support of strategic projects through the provision of innovation grants for foreign technology purchase", "the development of technology transfer network and participation in international programs on the development of science, technology and innovations", "Enhancement of technological and managerial competencies" (Government RK, 2014b).

The focus on science has sharpened since 2011, when the Law on Science was passed. This law recognises the importance of research and gives it priority along with science education. New types of higher education institutions called "research universities" were introduced. More recently, efforts to improve the quality of education, particularly of vocational training, have been introduced through the development of "points of growth" – selected new, world-class educational institutions in the area of secondary education, vocational training and tertiary education (OECD, 2016).

Involving businesses, including foreign ones, in developing and adjusting training and learning opportunities to the market needs would be a worthwhile effort. The government could consider incentivising firms to provide on-the-job training and learning opportunities, as well as providing apprenticeships, traineeships and internships. The OECD *Guidelines* call on enterprises to encourage local capacity building and human capital formation, in particular by creating employment opportunities and facilitating training opportunities for employees with a view to improving skills levels. Enterprises are encouraged to invest, to the greatest extent practicable, in training and lifelong learning while ensuring equal opportunities to training for women and other vulnerable groups, such as youth, low-skilled people, people with disabilities, migrants, older workers, and indigenous peoples (OECD, 2011).

Competition

The goal of competition policy is to promote market conditions in which the nature, quality, and price of goods and services are determined by competitive market forces. This benefits consumers and the economy as a whole, as well as enterprises through allowing them to respond efficiently to consumer demand. The OECD *Guidelines* recognise the importance of compliance with competition laws and regulations by domestic and foreign businesses.[13] Enterprises are

expected to carry out their activities in a manner consistent with all applicable laws and regulations and to refrain from entering into or carrying out anti-competitive agreements among competitors. An important aspect of enterprises responsibilities in this regard is co-operation with competition authorities and promotion of awareness and training among employees on the importance of compliance, particularly among senior management.

Competition policy of Kazakhstan is already discussed in Chapter 2 of the present *Review*. In terms of RBC, questions have been raised around the intersection between competition law and RBC standards developed at international level, with concerns being raised that competition law principles may chill RBC initiatives, particularly if these entail co-operating with other companies (and possibly competing companies) and participation in multi-stakeholder initiatives. A recent analysis by the OECD Secretariat *Competition Law and Responsible Business Conduct*, prepared for the 2015 Global Forum on Responsible Business Conduct, has found a variety of approaches in OECD countries on how to address the concerns that may be raised, detailing ways to avoid competition law issues in relation to RBC collaboration or initiatives, such as seeking advice and guidance from competition enforcers, practicing transparency and developing and implementing compliance programmes to ensure there is awareness of the risks and an understanding of how they should be managed at an organisational level (OECD, 2015d).

Taxation

Chapter 4 summarises the taxation policy framework in Kazakhstan. As related to RBC, tax governance and tax compliance should be treated as important elements of enterprise oversight and broader risk management systems and corporate governance. A comprehensive risk management strategy that includes tax not only allows the enterprise to act as a good corporate citizen but also to effectively manage tax risk, which can serve to avoid major financial, regulatory and reputation risk for an enterprise. The *Guidelines* call on enterprises to comply with both the letter and spirit of the tax laws and regulations of the countries in which they operate and make timely payments of their tax liabilities.

Corporate boards, in particular, have a role to play. The *Guidelines* recommend that boards should adopt tax risk management strategies to ensure that the risks associated with taxation are fully identified and evaluated. This entails proactively developing appropriate tax policy principles, as well as establishing internal tax control systems so that management actions are consistent with board views on tax risk. Businesses are also expected to co-operate with tax authorities and provide information that is required by law to ensure an effective and equitable application of the tax laws. This also

includes co-operation by multinational enterprises as related to transfer pricing and the arm's length principle.

Some governments provide incentives to encourage businesses to uptake responsible business practices, including financial incentives such as credits for demonstrated commitment to RBC in government contracting, procurement processes, investment or tax incentives (e.g. to encourage businesses to, for example, invest in low-carbon technologies, or to pursue a social objective). Kazakhstan provides exemptions from value added tax on sales of goods, works and services and corporate income tax, and a lowered social tax rate, for employers and entrepreneurs if at least 51% of the total number of employees are people with disabilities and if at least 51% of total expenditure on wages accounts for their employment.

In general, financial incentives, and, in particular tax incentives, need to be considered in the context of the overall tax system and taking into account their full costs and benefits. Such incentives could be an appropriate step once the baseline reforms establishing a more efficient tax system have been completed.

Policy recommendations

The legal framework that protects the public interest and underpins RBC has been partially established in Kazakhstan, but more efforts are needed to strengthen it further and ensure implementation and enforcement of the relevant laws. Awareness of RBC principles and standards is not yet widespread, but Kazakhstan's adherence to the *Declaration*, and, in particular, the formal establishment of an NCP under the *Guidelines*, will be an opportunity to consolidate existing efforts and further promote RBC principles and standards, both within the government and with the wider public.

- Develop a National Action Plan on Responsible Business Conduct, in collaboration with stakeholders and in line with international good practices. Clearly communicate expectations on RBC, provide guidance on accepted practices, and promote policy coherence and alignment on RBC. Support awareness raising events.
- Consider strengthening disclosure requirements for non-financial information in line with international best practice. Ensure, as a matter of policy coherence, that any corporate governance reforms adequately address, describe and reflect the extent of corporate responsibilities related to environmental and social matters.
- Ensure that the legal framework and national system of protection of human and labour rights is aligned with international standards. Make a particular effort to promote the good offices envisioned as part of the mandate of the NCP for the Guidelines as one of the available state-based non-judicial

mechanisms for resolving issues related to human rights and employment and labour relations.

- Include RBC expectations in FDI attraction efforts and include RBC criteria in efforts to promote linkages between MNEs and domestic industries, for example, by making RBC one element of supplier databases and matchmaking events. Include RBC principles and standards in industry-specific training programmes for local firms and support training and awareness-raising with business leaders on RBC.
- Involve the private sector in human resource development policies and encourage internal and external training by employers. Communicate to enterprises that contributing to human capital formation (in particular by creating employment opportunities and facilitating training opportunities for employees) is a pillar of RBC – and recognise those that do it.
- Increase the quality of institutions charged with environmental protection and promote compliance with internationally recognised standards as a competitive opportunity that could open up opportunities for international investment and trade.
- Continue the ongoing reforms to combat bribery and further encourage the development and implementation of preventive measures in the private sector.
- Consider introducing initiatives that promote consumer education and information programmes in order to increase the capacity of the civil society to be aware of consumer rights, to monitor government policy, and to promote effective protection of consumer rights. Particular efforts could be made to promote sustainable consumption.

Notes

1. For more information see *http://mneguidelines.oecd.org/database/instances/uk0036.htm* and the Initial Assessment by the UK NCP available at *https://www.gov.uk/government/publications/uk-ncp-initial-assessment-complaint-against-the-kpo-consortium-in-kazakhstan*.
2. See, for example, the outcomes of the international conference *Introducing standards of the responsible business conduct in politics and policy – national and international experience* (LPRC, 2015).
3. For more information refer to the *Report On The Implementation of the Recommendation On Due Diligence Guidance For Responsible Supply Chains Of Minerals From Conflict-Affected And High-Risk Areas, see the OECD website*.
4. 1) International Convention on the Elimination of All Forms of Racial Discrimination, 2) International Covenant on Civil and Political Rights; 3) International Covenant on Economic, Social and Cultural Rights; 4) Convention on the Elimination of All Forms of Discrimination against Women; 5) Convention against Torture and Other Cruel, Inhuman or Degrading Treatment or Punishment; 6) Convention on the Rights of the Child; 7) International Convention for the Protection of All Persons from Enforced

Disappearance; 8) Convention on the Rights of Persons with Disabilities. Kazakhstan has not ratified the International Convention on the Protection of the Rights of All Migrant Workers and Members of Their Families.

5. Fundamental conventions include 1) Forced Labour Convention, 1930 (No. 29); 2) Freedom of Association and Protection of the Right to Organise Convention, 1948 (No. 87); 3) Right to Organise and Collective Bargaining Convention, 1949 (No. 98); 4) Equal Remuneration Convention, 1951 (No. 100); 5) Abolition of Forced Labour Convention, 1957 (No. 105); 6) Discrimination (Employment and Occupation) Convention, 1958 (No. 111); 7) Minimum Age Convention, 1973 (No. 138); 8) Worst Forms of Child Labour Convention, 1999 (No. 182). Governance Conventions include 1) Labour Inspection Convention, 1947 (No. 81); 2) Employment Policy Convention, 1964 (No. 122); 3) Labour Inspection (Agriculture) Convention, 1969 (No. 129); 4) Tripartite Consultation (International Labour Standards) Convention, 1976 (No. 144).

6. The limited power of the Ombudsman to stop human rights abuses has also been noted by the domestic civil society and some international human rights defenders. Questions have also been raised about the Ombudsman's limited mandate, as well as its independence. See for example the 2015 Human Rights Report by the US Department of State, *www.state.gov/documents/organization/253177.pdf*, or the Amnesty International 2015 country report, *www.amnesty.org/en/countries/europe-and-central-asia/kazakhstan/report-kazakhstan/*.

7. This document is only available in Russian.

8. The exact number of deaths and casualties is disputed.

9. See UN (2015); EU Statement on Legal and Judicial Reforms in Kazakhstan: *www.osce.org/pc/121302?download=true*; US Mission to OSCE Statement on Kazakhstani Criminal Code: *www.osce.org/pc/121082?download=true*.

10. A full submission on documents regarding this review is available at *CCPR – International Covenant on Civil and Political Rights, 117 Session (20 Jun 2016-15 Jul 2016), http://tbinternet.ohchr.org/_layouts/treatybodyexternal/SessionDetails1.aspx?SessionID=1031&Lang=en*.

11. The government has reported that the Ministry of Education and Science provides a "Bolashak" international scholarship for higher education degrees and scientific and industrial internships for priority sectors of the economy.

12. See the country report by the US Department of State Trafficking in Persons Report 2016, *www.state.gov/j/tip/rls/tiprpt/2016/index.htm*; US Department of Labor 2014 Findings on the Worst Forms of Child Labor, *www.dol.gov/sites/default/files/documents/ilab/reports/child-labor/findings/2014TDA/kazakhstan.pdf*; and the US Department of Labor List of Goods Produced by Child Labor or Forced Labor, *www.dol.gov/ilab/reports/child-labor/list-of-goods/*.

13. For example, the recent sentencing of a former high-level official that headed the Astana EXPO 2017 company and was found guilty of embezzling KZT 10.2 billion (USD 30 million) (Eurasianet, 2016).

14. The term competition law in the OECD *Guidelines* is used to refer to laws, including both antitrust and antimonopoly laws, that variously prohibit: a) anti-competitive agreements; b) the abuse of market power or of dominance; c) the acquisition of market power or dominance by means other than efficient performance; or d) the substantial lessening of competition or the significant impeding of effective competition through mergers or acquisitions.

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Annex A

Kazakhstan's exceptions to national treatment in the meaning of the OECD Declaration on International Investment and Multinational Enterprises

A. Exceptions at national level

I. Investment by established foreign-controlled enterprises

Agricultural land and forests

Foreign natural and legal persons and foreign-established enterprises where the share of foreign equity participation is more than 50% cannot own agricultural land plots. They are entitled to lease agricultural land plots for up to 10 years, while Kazakh legal entities and citizens can lease agricultural land for up to 49 years. Foreign natural and legal persons cannot own forests.

Authority: Land Code of Kazakhstan of 20 June 2003 (Articles 23, 24 and 37).

Telecommunications services

In order to directly or indirectly own, use, dispose of or manage an aggregate of more than 49% of the voting shares in a legal entity supplying long-distance and international telecommunications services and owning terrestrial communications lines (cable, including optical fibre and radio relay), foreign investors must obtain a special approval from the Government. This approval is based on recommendations from the Ministry of Information and Communication and the National Security Committee.

Authority: Law on National Security No. 527-IV of 6 January 2012, as amended (Article 23).

Mass media

Direct or indirect foreign ownership (ownership by a foreigner or a foreign legal entity) in the media sector is limited to 20% of the share capital.

Authority: Law on National Security No. 527-IV of 6 January 2012, as amended (Article 23).

Security services

Foreigners, foreign legal entities and established foreign-controlled enterprises shall not provide security services or manage companies providing security services.

Authority: Law No. 85 "On Security Services" dated 19 October 2000 (Article 5).

II. Official aids and subsidies

None.

III. Tax obligations

None.

IV. Government purchasing

None.

V. Access to local finance

None.

B. Exceptions at the level of territorial subdivisions

None.

ANNEX B

Measures notified by Kazakhstan for transparency in the meaning of the OECD Declaration on International Investment and Multinational Enterprises

A. Measures reported for transparency at the level of national government

I. Measures based on public order and essential security considerations

a) Investments by established foreign-controlled enterprises

Cross-sectoral. Pursuant to the 2012 National Security Law, which takes a broad definition of national security by encompassing economic security, foreign investment activities can potentially be limited or banned in unidentified areas due to national security considerations. Furthermore, in accordance with the Civil Code and the Law on State Property, discriminatory decision may be taken by the government which may restrict the freedom of owners of strategic objects, defined as a property of social and economic importance, to sell them to locally-established foreign-controlled enterprises.

Authority: Law on National Security No. 527-IV of 6 January 2012, as amended; Civil Code (Article 193-1); and Law on State Property No. 413-IV of 1 March 2011, as amended (Article 188-3).

Agricultural land in border areas. Agricultural land immediately adjacent (3-km zone) to the protected zone of the state border of the Republic of Kazakhstan can only be leased by citizens and legal entities of the Republic of Kazakhstan. Foreigners and foreign legal entities shall not lease or own agricultural land in this zone.

Authority: Land Code dated 20 June 2003 No. 442-II, as amended (Articles 23 and 24).

b) Corporate organisation

None.

c) Government purchasing

None.

d) Official aids and subsidies

None.

II. Other measures reported for transparency

a) Corporate organisation

Cross-sectoral. Foreigners are prohibited to establish as individual entrepreneurs.

Authority: Entrepreneurial Code of the Republic of Kazakhstan No. 375-V of 29 October 2015.

Maritime transport. Under the Shipping Law, cabotage shall be performed by vessels flying the national flag or the flag of another country (Caspian sea country) subject to authorisation by the government.

Authority: Law of the Republic of Kazakhstan No. 284-II "On Merchant Shipping" of 17 January 2002. Law of the Republic of Kazakhstan No. 574-II "On Inland Water Transport" of 6 July 2004.

Banking, insurance and other financial services. Foreign banks and insurance companies as well as foreign companies providing brokerage services are not allowed to open branch offices. They may open a representative office with the permission of the competent authority.

In accordance with the Law No. 422-V ZRK "On amendments and addenda to certain legislative acts of the Republic of Kazakhstan on the issues of non-performing loans and assets of the second-tier banks; on rendering financial services and activities of the financial institutions and the National Bank of the Republic of Kazakhstan" of 24 November 2015 starting from 16 December 2020 non-resident banks, insurance (reinsurance) companies and companies providing brokerage services will be allowed to open a branch in the territory of Republic of Kazakhstan, subject to terms and conditions established by the legislation of the Republic of Kazakhstan taking into account commitments undertaken in the Schedule of specific commitments on trade in services.

Authority: Law of the Republic of Kazakhstan No. 2444 of 31 August 1995 "About banks and banking activity in the Republic of Kazakhstan, as amended; Law of the Republic of Kazakhstan No. 126-II of 18 December 2000 "On insurance activities", as amended; Law No. 422-V "On amendments and addenda to certain legislative acts of the Republic of Kazakhstan on the issues of non-performing loans and assets of the second-tier banks; on rendering financial services and activities of the financial institutions and the National Bank of the Republic of Kazakhstan" of 24 November 2015.

Banking and insurance. Resident and non-resident legal entities (as well as individuals) may act as founders, or be shareholders of local insurance companies or banks. However, entities registered in certain offshore countries determined by the Government (listed in Resolution No. 145 dated 2 October 2008, as amended), or their individual shareholders cannot be founders or shareholders of a local insurance company or a bank. This restriction does not however apply to insurance companies or banks that have a minimal international credit rating of BBB or equivalent (foreign currency rating, international scale).

Authority: Banking Law No. 2444 adopted on 31 August 1995, as amended (Articles 29 and 17), and Resolution No. 385 of the National Bank of Kazakhstan (24 December 2012), as amended; Law on insurance companies No. 126-II adopted on 18 December 2000, as amended (Articles 33 and 21); Resolution No. 145 dated 2 October 2008 of the Board of Agency of Republic of Kazakhstan on Regulation and Supervision of Financial Market and Financial Organisations "On approval of the list of offshore zones for the purposes of banking and insurance activities, activities of professional participants of securities market and other licensed types of activities in the securities market, activity of accumulative pension funds and joint stock investment funds", as amended.

Other finance. Resident and non-resident legal entities (as well as individuals) can set up and be shareholders of companies providing specialised services on financial markets (securities dealing, stock brokerage services, underwriting new issues) and of investment funds, provided they are not controlled by legal entities registered in offshore jurisdictions (as listed in the Government Resolution No. 145). This restriction does not apply to companies that are subsidiaries of non-resident companies that have a minimum long-term credit rating of BBB on foreign currency (as rated by international ratings agencies listed in Resolution No. 385).

Authority: Law on Securities No. 461 adopted on 2 July 2003, Article 47, paragraph 2 and Law on investment funds No. 576-II adopted on 7 July 2004, Article 2 paragraph 8. Resolution No. 385 of the National Bank of Kazakhstan dated 24 December 2012, as amended.

Non-resident asset management companies can offer asset management services for pension funds if they respect minimal financial rating criteria and are not controlled by entities from offshore jurisdictions.

Authority: Law on Pension Provision No.105-V adopted on 21 June 2013, as amended.

b) Key personnel

Cross-sectoral. Limits on employment of foreign staff apply to each employee category. There are four categories for which the permits' issuance and renewal conditions are defined: executive and their deputies (Category I), managers and specialists (Category II); specialists (Category III); and skilled workers (Category IV):

- Foreign staff in the first (executives and their deputies) and second (managers and specialists) categories is limited to 30 %;
- Foreign staff in the third (specialists) and fourth (qualified workers) categories is limited to 10%.
- In addition, the number of foreign transferees (i.e. foreigners transferred in a Kazakh affiliate of their employer) shall be not more than 50% of the relevant staff category (managers and specialists) in each company (with respect to executives, this limitation does not apply).

Authority: Law of the Republic of Kazakhstan "On Employment" No. 482-V dated 06 April 2016; the Government Decree of the Republic of Kazakhstan of 13 January 2012 No. 45 "Rules and conditions for Hiring Foreign Workers" (as last amended on 31 March 2016); the Law of the Republic of Kazakhstan No. 477-IV "On Migration of Population" of 22 July 2011 (as last amended on 6 April 2016); the Law of the Republic of Kazakhstan No. 2337 "On the Legal Status of Foreigners" of 19 June 1995 (as last amended on 24 November 2015).

Sector-specific. Certain professional activities can be performed by citizens of Kazakhstan only:

Maritime transport. Foreign persons cannot take the position of the captain, chief captain's mate, chief engineer and signaller of a ship.

Authority: Law of the Republic of Kazakhstan No. 284-II "On Merchant Shipping" of 17 January 2002; Law of the Republic of Kazakhstan No. 574-II "On Inland Water Transport" of 6 July 2004.

Air transportation. Only a citizen of the Republic of Kazakhstan may be the head of the aviation security service of airport or an air company providing scheduled air transport services. Only a citizen of the Republic of Kazakhstan can be the air security officer of an operator providing non-scheduled air services and aerial works.

Authority: Law of the Republic of Kazakhstan No. 339-IV "On Use of Air Space and Air Operations" of 15 July 2010.

Tourism. Only a citizen of the Republic of Kazakhstan can work as a guide (interpreter guide) or tourism instructor.

Authority: Law of the Republic of Kazakhstan No. 211-II "On Tourist Activity in the Republic of Kazakhstan" of 13 June 2001.

Legal and para-legal services . Only a citizen of the Republic of Kazakhstan may be an advocate or a candidate advocate (intern).

Only a citizen of the Republic of Kazakhstan can be a notary or a candidate notary (intern).

Only a citizen of the Republic of Kazakhstan may be a patent attorney.

A public or a private bailiff can only be a citizen of the Republic of Kazakhstan.

Authority: Law of the Republic of Kazakhstan No. 195-I "On Advocacy" of 5 December 1997; Law of the Republic of Kazakhstan No. 155-I "On Notariat" of 14 July 2007; Patent Law of the Republic of Kazakhstan No. 427-I of 16 July 1999; Law of the Republic of Kazakhstan No. 261-IV "On Enforcement Proceedings and Bailiff Status" of 20 April 2010.

Forensic. Only a citizen of the Republic of Kazakhstan can be a forensic expert in forensic enquiry bodies.

Authority: Law of the Republic of Kazakhstan No. 240-IV "On Forensic Examination Activity in the Republic of Kazakhstan" of 20 January 2010.

c) Government purchasing

Government procurement is open to non-resident foreign enterprises and domestic economic operators on equal grounds, provided that the requirement to grant such a regime is set by the international treaties ratified by the Republic of Kazakhstan and pursuant to the terms and conditions set forth in such treaties. Currently Kazakhstan provides national treatment for the purposes of participation in public procurements only for the Member-States of the Eurasian Economic Union (Armenia, Belarus, Kyrgyzstan and Russia) under the Treaty on Eurasian Economic Union of 29 May 2014 on a reciprocity basis.

Authority: Law "On Public Procurement" N° 434-V of 4 December 2015 (subparagraph 31 of Article 2, and Article 14).

d) Official aids and subsidies

None.

B. Measures reported for transparency by territorial subdivisions

None.

C. Monopolies and concessions

At the national level

I. Public monopolies

- Maintaining State land cadastre of the Republic of Kazakhstan;
- Forestry, connected with inventory of forest resources and territorial set up of the forest fund;
- Conducting meteorological and hydrological monitoring and monitoring the condition of the environment;
- Expertise of pharmaceutical products, medical devices and of medical equipment;
- Evaluation of safety and quality of pharmaceutical products, medical devices registered in the Republic of Kazakhstan;
- Registration of the pledge on movable property, not subject to mandatory State registration;
- Determination of the cost of taxation objects (housing, country cottage building, object of unfinished construction, unheated extension, household (service) building, basement level, cellar of the housing, garage);
- State technical inspection of buildings, constructions, and (or) their components;
- Localization and liquidation of epicentres of dissemination of quarantine objects;
- In the field of protection of selective achievements accepting and conducting preliminary expertise of applications for selective achievements;
- In the field of protection of inventions, utility models, industrial design acceptance and expertise of applications for inventions, utility models and industrial designs;
- In the field of protection of trademarks, service marks, appellations of origin acceptance and expertise of applications for registration of trademarks, service marks, and appellations of origin;
- Conducting comprehensive outsourced expertise of construction drafts (of technical and economic justifications and of design-and-estimate documentation);
- Maintaining State city-planning cadastre;
- In the field of veterinary diagnostics of extremely hazardous and enzootic animal diseases;

- In the field of electronic document and electronic digital signature activity of the trusted third party of the Republic of Kazakhstan on conducting verification of authenticity of the foreign electronic digital signature, activity of the national validating centre;
- In the field of communications technical support of works on monitoring of radio-frequency spectrum and radio-electronic tools;
- In the field of informational development attestation inspection of informational system, informational-communication platform of "electronic government" and internet resource of the State body on their compliance with requirements of informational security;
- In the field of mandatory social insurance personified recording and formation of centralized data base of mandatory social expenditures and social payments of participants of the system pf mandatory social insurance; organisation of social payments from the State fund of social insurance;
- In the field of State statistics collection, processing of the primary statistical data, their storage in electronic format; formation, support and actualization of informational-statistical systems, databases and their platforms, registries of statistics, internet-resource of the authorized body;
- Preparation of identity documents, accumulation and maintenance of the integrated data pool of the system of document preparation, automatization of the work on recording of migration processes, elaboration, implementation and support of software-technical products for internal affairs bodies;
- Withdrawal of sturgeon species from natural habitat, their purchase, processing, and export of their roe and of other types of products;
- Organizing methodological and scientific-methodological support of the education system and educational process (State mandatory public standards of education, curriculums, education programs);
- Organizing expertise of textbooks, educational-methodical kits and handbooks by levels of education.

Authority:

- Land Code of the Republic of Kazakhstan No. 442 of 20 June 2003
- Forest Code of the Republic of Kazakhstan No. 447 of 8 July 2003
- Environmental Code No. 212 of 9 January 2007
- Code of the Republic of Kazakhstan «On Public Health and the System of Healthcare» No. 193-IV of 18 September 2009
- Law of the Republic of Kazakhstan «On Registration of The Pledge on Movable Property» No. 254 of 30 June 1998
- Law of the Republic of Kazakhstan «On Valuating Activity in the Republic of Kazakhstan» No. 109 of 30 November 2000

- Law of the Republic of Kazakhstan «On State Registration of Rights for Immovable Property» No. 310 of 26 July 2007
- Law of the Republic of Kazakhstan «On Quarantine of Plants» No. 344 of 11 February 1999
- Law of the Republic of Kazakhstan «On Protection of Selective Achievements» No. 422-I of 13 July 1999
- Law of the Republic of Kazakhstan «Patent Law of the Republic of Kazakhstan» No. 427 of 16 July 1999
- Law of the Republic of Kazakhstan «On Trade Marks, Service Marks, and Appellations of Origin» No. 456 of 26 July 1999
- Law of the Republic of Kazakhstan «On Architectural, City Planning and Construction Activity in the Republic of Kazakhstan» No. 242 of 16 July 2001
- Law of the Republic of Kazakhstan «On Veterinary» No. 339 of 10 July 2002
- Law of the Republic of Kazakhstan «On Electronic Document and Electronic Digital Signature» of 7 January 2003 No. 370
- Law of the Republic of Kazakhstan « n Communications» No. 567 of 5 July 2004
- Law of the Republic of Kazakhstan «On Informational Development» No. 418-V of 24 November 2015
- Law of the Republic of Kazakhstan «On Mandatory Social Insurance» No. 405 of 25 April 2003
- Law of the Republic of Kazakhstan «On State Statistics» No. 257-IV of 19 March 2010
- Law of the Republic of Kazakhstan «On Identity Documents» No. 73-V of 29 January 2013
- Law of the Republic of Kazakhstan «On Protection, Reproduction, and Use of Animal World» No. 593 of 9 July 2004
- Law of the Republic of Kazakhstan "On Education" No. 319-III of 27 July 2007.

II. Natural monopolies

- Transportation of oil and/or oil products via mainline pipelines, except in the cases of their transportation for the purposes of transit through Kazakhstan and export out of Kazakhstan;
- Storage, transportation of commercial gas via connecting, main line gas pipelines and /or gas distribution facilities, exploitation of group reservoir units, and transportation of crude gas via connecting pipelines, , except in

the cases of storage, transportation of commercial gas with the aim of transit through Kazakhstan and export out of Kazakhstan;

- Electric power transmission and/or distribution;
- Thermal energy production, transmission, distribution and/or supply, except for thermal energy generated with the use of soil heat, from underground water, rivers, water reservoirs, discharge water of industrial enterprises and power stations, and from sewers;
- Technical dispatching of electric power grid output and consumption;
- management of the balancing of electric power grid;
- Mainline railway networks, except for mainline railway network services in transportation of goods in containers and transportation of empty containers;
- Railway track services with the objects of railway transport under concession agreements in the absence of alternative railway track;
- Approach track services in the absence of alternative approach track ;
- Air navigation;
- Ports, airports;
- Provision or lease of underground cable systems and other fixed assets related to connection of telecommunication networks to the public telecommunication networks;
- Universal postal services;
- Water-utilisation and/or sewer systems;

Authority: Article 4, Law No. 272 "On Natural Monopolies and regulated markets" (9 June 1998), as amended. The Law also refers to Order No. 186 of the Minister of Economy (30 December 2014), which provides a detailed list of natural monopolies.

III. Private monopolies

None.

IV. Concessions

Exploration and exploitation of oil and gas negotiated by Subsurface users with the Government (must comply with the provisions of the Subsurface Law).

Authority: Subsurface exploration and exploitation contracts are regulated by the 2010 Subsurface Law (Law No. 291-IV adopted on 24 June 2010), as amended. See Articles 61 to 74 on Subsurface users' contracts.

Infrastructure facilities in all economic sectors can be the object of a concession agreement, except for trunk rail networks, navigable waterways,

lighthouses and other navigation devices & signs, and water structures (dams, hydroelectric and other hydraulic structures). Kazakhstan allows the concession of water management facilities (water intake facilities, pumping stations, water treatment facilities) of most large cities.

Authority: Law on Concessions (No. 167-III) adopted on 7 July 2006 (Article 4), as amended, and corresponding list of objects which cannot be transferred into concession (Decree of the President No. 294 adopted on 5 March 2007).

At the level of territorial subdivisions

None.

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This review, which was prepared in response to Kazakhstan's 2012 request to adhere to the Declaration on International Investment and Multinational Enterprises (OECD Declaration), analyses the general framework for investment as well as most recent reforms, and shows where further efforts are necessary. It assesses Kazakhstan's ability to comply with the principles of openness, transparency and non-discrimination and its policy convergence with the OECD Declaration, including responsible business conduct practices. Capitalising on the OECD Policy Framework for Investment, this review studies other policy areas that are of key relevance to investment such as SME policy, infrastructure development, trade policy as well as anti-corruption efforts. Since the first review of Kazakhstan, in 2012, the authorities have made strides in opening the country to international investment and in improving the policy framework for investment as part of their efforts to diversify the economy to avoid continued overreliance on oil. Additional policy measures are nevertheless required to create a stimulating environment for investment if the government wants to fulfil its goal of economic diversification and sustainable development.

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