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# Overview of the new Law “On transfer pricing” in Kazakhstan

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# What is a “transfer price”?

- OECD definition:

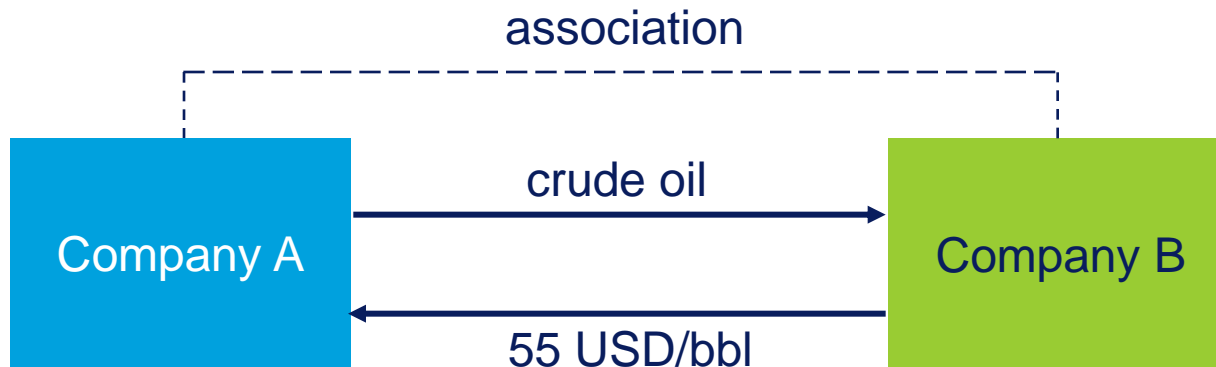
**Transfer price** is the price at which

an enterprise transfers (sells)

physical goods / intangible property / provides services

to an **associated enterprise** (related party).

*Example:*



# What is “association”?

- OECD definition:

## **Associated enterprises:**

- one of the enterprises participates directly or indirectly in the management / control / capital of the other

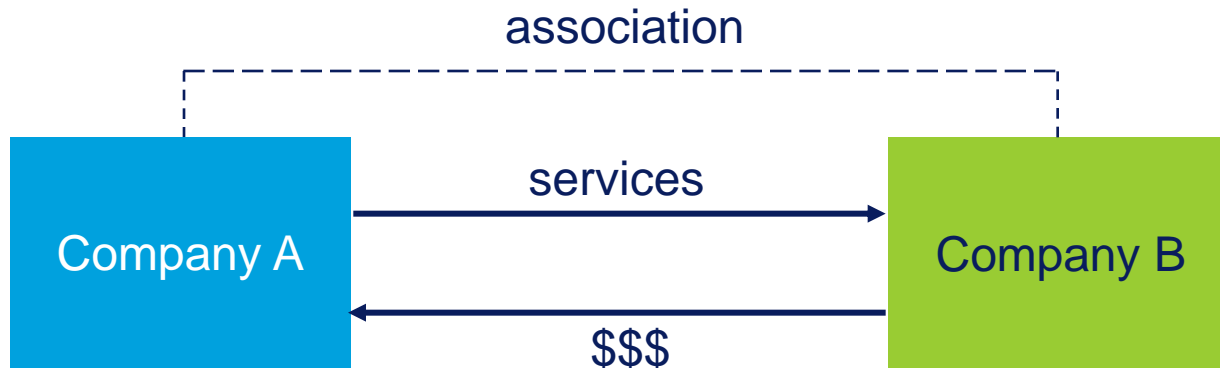
*Example:* a parent company and its subsidiary

or

- the same person(s) participate directly or indirectly in the management / control / or capital of both enterprises

*Example:* two sister companies, i.e. two enterprises under common control

# How TP works (for tax purposes)



- Company A:

price ↑ - revenue ↑ - taxable income ↑ - income tax ↑

- Company B:

price ↑ - deductible expenses ↑ - taxable income ↓ - income tax ↓

# Stages of the legislative reform in Kazakhstan

- Working group on preparation of amendments to improve normative-legal acts regulating transfer pricing issues (2004-2006)
- Draft of the new Law “On state control over application of transfer prices”
  - Introduced to *Majilis* of the Parliament by the Government resolution of 24 April 2006
- The new Law “On transfer pricing” (further, the “New Law”)
  - enters into force on 1 January 2009
  - supersedes the Law “On the state control over the application of transfer pricing” of 5 January 2001

# Definition of the transfer price and related parties

- Transfer price
  - is the price that is established between related parties and/or differs from the objectively established market price
- Related parties
  - parties having special relations which include, among other conditions, situations when “the parties to a transaction use the transaction price deviating from the market price”

# Transactions subject to transfer pricing regulations

- International business transactions:
  - export and import of goods
  - work performance and service provision to which one of the parties is a non-resident operating in Kazakhstan without a permanent establishment (new)
  - operations performed by Kazakhstan residents outside of Kazakhstan including sale and purchase of goods, performance of work and provision of services (new)

# Transactions subject to transfer pricing regulations

- Transactions in the territory of Kazakhstan “directly related” to international business transactions:
  - transactions in minerals being sold that were produced by a subsurface user who is a party to the transaction (new)
  - transactions where one counterparty uses tax benefits
  - transactions where one counterparty has a loss according to the tax returns for the two tax periods preceding the year of the transaction

# Methods for determining market price

- Comparable uncontrolled price method
  - internal comparables
  - external comparables
- Cost plus method
- Resale price method

# Methods for determining market price

- Profit split method - determines the profit derived from the transaction which is to be allocated between the transaction parties based on:
  - economic feasibility
  - functional analysis, agreements entered into according to the arm's length principle
  - based on the profits these companies would receive if they were independent
- Net margin method - is based on the determination of the net revenue, which would be derived from this transaction by unrelated parties under comparable economic conditions

# Methods for determining market price

- Price range - two or more market prices:
  - published in the official sources of informationor in absence of such prices
  - determined in accordance with the arm's length principle by means of one of the methods of market price determination pursuant to the procedure established by the Law
- Price range will replace the 10% price deviation threshold

# Sources of information used for market price determination

1. Officially recognized sources of information on the market prices
2. Sources of information on the exchange quotations
3. Data of state bodies, authorized bodies of other countries and organizations on prices, differential, costs and conditions affecting the deviation of the transaction price from the market price
4. Information programs used for the transfer pricing purposes, information granted to the transaction participants and other sources of information

# Requirements for reporting and documenting

- Monitoring of transactions in certain types of goods
  - The list of goods transactions in which are subject to monitoring is to be established by the Government
  - Rules for monitoring and monitoring compliance forms are to be developed and approved by the authorized bodies
  - When, as a result of monitoring, it is established that the transaction price deviates from the market price, the authorized bodies will conduct a transfer pricing audit
- With respect to the transactions in goods which are not subject to monitoring, the taxpayers should keep documentation justifying the price used and submit it to the authorized bodies upon request

# Advance pricing agreements

- Agreements on transfer pricing application
  - is entered into by transactions parties and authorized bodies
  - should be executed as a written agreement between the authorized bodies and the transaction party
  - establishes for a certain period a method for market price determination and the source of information to be used for this purpose

# Transfer pricing adjustments

- Adjustments to objects of taxation and objects related to taxation:
  - are made if such adjustments results, or may subsequently result, in increase of tax and other obligatory payments to the budget
  - exception is the transactions approved by the authorized bodies that do not violate the price regulations in certain cases
  - break off application of benefits for payment of tax or customs duties in the periods when the taxpayer is deemed to apply prices inconsistent with market prices

# Transfer pricing normative acts

- The tax authorities have started drafting the following set of documents required for application of the New Law:
  - instruction on transfer pricing control over international transaction (to be approved by the tax and customs authorities)
  - the list of stock exchange commodities (to be approved by the Government)
  - the list of official sources of information (to be approved by the Government)
  - the list of types of commodities subject to monitoring (to be approved by the Government)

# Our main transfer pricing services

- Risk analysis:
  - Evaluation of tax risks related to potential transfer pricing adjustments – for purposes of taxation, internal controls, audit or due diligence
  - Recommendations on the mitigation of transfer pricing related risks
  - Comparables searches
  - Collection of documents and development of a strategy to support consistency of transaction prices with market prices
- Planning and restructuring:
  - Advice on methodology and mechanisms of price setting, recommendations on drafting and concluding contracts
  - Design of an effective business structure for tax and transfer pricing purposes
  - Development of internal transfer pricing policies and procedures
  - Transfer pricing workshops and technical trainings for in-house personnel

# Our main transfer pricing services

- Position defense:
  - Preparation of comments with respect to transfer pricing issues in response to authorities' requests
  - Advisory assistance during transfer pricing audits
  - Development of the company's defense strategy and appropriate argumentation in case of disputes
  - Preparation of appeals resulting from transfer pricing audits
  - Participation in negotiations with the tax authorities to resolve disputes and coordinate positions
  - Representation of company's interests in resolving tax disputes in court

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