



TP Spotlight

No1 – July 2020

**Upcoming deadline for
Local File submission**

Transfer pricing Hotline: +7 771 781 8828

Consulting on transfer pricing issues

kpmg.kz



Dear Readers,

We are delighted to be able to bring to your attention this general overview of recent changes in Kazakhstan's Transfer Pricing legislation; changes that could influence the activities of your business in Kazakhstan.

Upcoming deadline for Local File submissions: 31.12.2020

At the end of 2017, Kazakhstan's transfer pricing legislation underwent significant change. Following international practice, provisions relating to how international groups do their reporting were adopted. ¹Specific criteria were established for members of international groups concerning their obligation to provide one or more Transfer Pricing Reporting Forms, such as:

1. A Notification on their Membership of an International Group (the Notification);
2. A Local File;
3. A Master File;
4. A Country by Country Report (the CbyC Report).

Since 2019, taxpayers have been subject to administrative liability for failing to submit certain Transfer Pricing Reporting Forms.

The reporting requirements for international groups were introduced in stages. The CbyC Report was introduced retrospectively from 1 January 2016, and the first reporting period for Local Files and Master Files was 2019. The Local File for 2019 should be submitted to the tax authorities no later than 31 December 2020. The Master File must be provided by a member of an international group within the 12 months following receipt of a request to do so by the tax authorities.

Notification submission deadline – 1 September 2020

The following member firms of international groups are required to file Notifications:

- the ultimate parent company of an international group resident in Kazakhstan;
- an authorised participant or other member of an international group, if there is an obligation or request to submit a Local File, Master File or CbyC Report.

The Notification must be submitted annually, but no later than 1 September of the year following the reporting financial year. It must be submitted by those members of an international group that are subject to the obligation or request to submit at least one of the above Transfer Pricing Reporting Forms.

Local File submission deadline – 31 December 2020

The obligation to submit a Local File lies on the following member firms of an international group:

- the ultimate parent company of an international group resident in Kazakhstan;
- an authorised participant in an international group;
- another resident of Kazakhstan, but not one that is an ultimate parent company or authorised participant in an international group;
- a non-resident that performs business activities in Kazakhstan via a structural division and/or a permanent establishment,
- if the following conditions are met simultaneously:
 - the member of the international group performed the transaction in the reporting financial year, and this transaction is subject to transfer pricing scrutiny;
 - the revenue of the member firm of an international group for the financial year preceding the reporting financial year is at least five million Monthly Index Factors (MIF), which is about 12 billion tenge. In other words, for there to be an obligation to submit the Local File for 2019 by 31 December 2020, the taxpayer's revenue according to its financial statements for 2018 should exceed the threshold established above.

Controversial issues

The anticipated changes

The Order of the Minister of Finance of the Republic of Kazakhstan of 24 December 2018 approved the Forms and Rules for completing Local File, Master File and CbyC Reporting. These Forms and Rules took effect on 1 January 2019.

The Ministry of Finance has now submitted draft amendments to the Forms and Rules for completing Transfer Pricing Reporting Forms .

In addition to the editorial amendments, the draft law envisions significant change to applied definitions, the determination of the materiality of a transaction, and the content of the Local File and how it is to be filed. Notably the draft:

¹ Law No. 122-VI of the Republic of Kazakhstan "Amending Certain Legislative Acts of the Republic of Kazakhstan Related to Taxation Issues", dated 25 December 2017

Expected changes

The Order of the Minister of Finance of the Republic of Kazakhstan of 24 December 2018² approved the Forms and Rules for completing Local File, Master File and CbyC Reporting. These Forms and Rules took effect on 1 January 2019.

The Ministry of Finance has now submitted draft amendments to the Forms and Rules for completing Transfer Pricing Reporting Forms³.

- clarifies the definition for a controlled transaction. A transaction is recognised as controlled if it is performed by a member of an international group with a related party;
- eliminates the provision on comparable economic conditions when determining the category of a controlled transaction;
- introduces a threshold for transaction materiality that considers the total amount of income (expenses) and/or liabilities in that category of controlled transaction (a threshold of 50,000 to 250,000 MIF is being discussed (the final version has not yet been adopted));
- introduces the possibility of submitting a Local File in electronic form.

Participation in an international group

If a company participates in an international group, it could have an obligation to prepare Transfer Pricing Reporting Forms. However, in some cases, recognizing a company as a member of an international group is unclear. For example:

- Is the group to which the company belongs considered as an international group?
- What characteristics of the group define it as an international group?
- Should the group be recognised as an international group only due to its consolidated financial statements, prepared when it issued shares on a securities exchange?

Revenues

One of the criteria for determining whether the member of an international group is obliged to prepare and submit a Local File is whether there is revenue of more than 5 million MIF, calculated using IFRS. If it is considered necessary to calculate the consolidated revenue of the ultimate parent company to determine whether it is obliged to prepare a Master File or CbyC Report, the question may arise regarding which indicators must be selected to measure revenue.

Definition of controlled transaction

The law states that a member of an international group must submit a Local File if it performs cross-border (and/or related) business transactions. At the same time, cross-border transactions under the Transfer Pricing Law will include ALL export and import transactions and transactions on the performance of work (provision of services), if one of the parties to the transaction is a non-resident operating in Kazakhstan without a permanent

² Order No. 1104 of the Minister of Finance of the Republic of Kazakhstan, dated 24 December 2018

³ On Approving the Forms for Local File, Master File and CbyC Transfer Pricing Reporting Forms, and the Rules for Their Completion



establishment. In other words, both intra-group transactions with non-residents, and non-residents which are not members of a group (independent companies) pursuant to Clause 15 of Article 11 of the Transfer Pricing Law, are subject to transfer pricing scrutiny.

The following issues remain open:

- whether the existence of transactions that are subject to transfer pricing scrutiny but have been performed with companies outside the group (independent companies) leads to an obligation on the taxpayer to prepare a Local File (for example, in the situation when a company is a member of an international group but does not have intra-group transactions); and
- whether the Kazakh resident company should disclose in the Local File transactions that are subject to transfer pricing scrutiny but have not been performed with group companies.

The proposed amendments do not give a clear answer to these questions, since according to the Transfer Pricing Law, one of the criteria for recognising that the parties to a transaction are related is how much the transaction price deviates from the arm's length range of prices as calculated by the relevant authorities.

Categories of transactions

It is proposed that transactions be categorised using the principle of identity and/or homogeneity, or according to identical or homogeneous characteristics. The concepts of identity/homogeneity consider physical, qualitative characteristics of goods/services, their reputation, place of origin and other financial and economic aspects. This categorisation leads to a broad interpretation of category definitions in transactions by both taxpayers and the tax authorities. For example, regarding transactions with commodities, there is practice that uses the Unified Commodity Classification of Foreign Trade Activity (ТН-ВЭД) as a mechanism for determining the transaction perimeter. However, the Unified Commodity Classification of Foreign Trade Activity could combine within one classification code various commodities that are not identical or homogeneous to those analysed within a transaction, which could be carried out in different economic conditions. Thus, subjectivity when determining different categories of controlled transaction remains.

Determination of materiality

The proposed amendments aim to bring the provisions of Kazakh transfer pricing legislation in line with international practice. In various jurisdictions the materiality threshold for the analysis of controlled transactions can be established in the form of relative ratios (for example, as a percent of revenues/expenses) and/or absolute amounts (fixed amounts). For example, in Belgium, the materiality level for transactions to be analysed in a Local File is EUR

one million; in Russia, it is RUB 60 million for cross-border transactions and RUB one billion for transactions between residents; and in Ukraine it is UAH ten million. In Poland, it all depends on the subject of the transaction.

However, in the proposed version, it remains unclear how the established threshold should be applied to controlled transaction categories. For example, support services that are not the core activity of a group are common in international groups. These support services may include services of a different nature and, consequently, the question arises concerning the application of materiality thresholds to the aggregate turnover for such services, or to each individual service under a support service contract.



Transfer Pricing Tips: Where to Start?

When preparing a Local File we recommend that you:



Analyse the structure of the group and the grounds for its recognition as an international group;



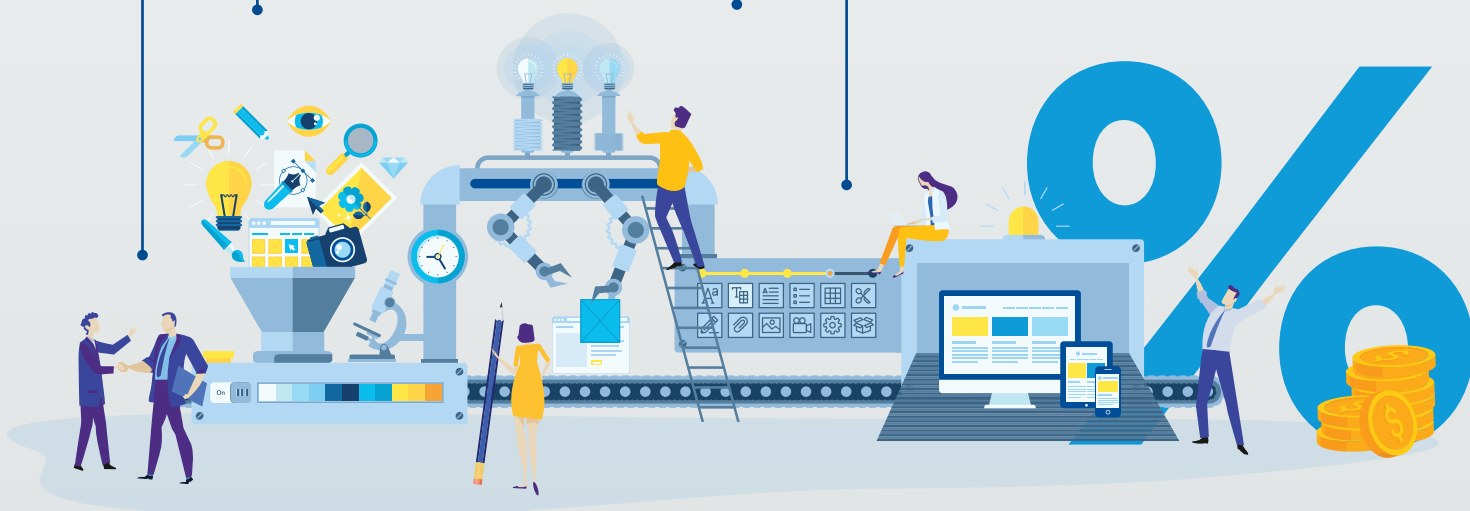
- pay attention to the subject of the transactions grouped in categories and, in the case of complex contracts, to the nature of the transaction itself;
- the Unified Commodity Classification of Foreign Trade Activity may be used as a starting point for categorising transactions with goods;
- emphasise homogeneity when analysing works and services, for example consulting, management and accounting services;



Determine the controlled transaction categories by grouping identical and/or homogeneous goods (work, services) for each individual counterparty;



Determine the aggregate income (expense) and/or liability for controlled transaction categories.



Contacts



Inna Alkhimova
Head of Tax and Legal
Partner
T: +7 727 298 08 98
E: ialkhimova@kpmg.kz



Vyacheslav Sosnovskiy
Tax and Legal
Director
T: +7 727 298 08 98
E: vsosnovskiy@kpmg.kz

KPMG Transfer pricing Hotline: +7 771 781 8828

kpmg.kz

The information contained herein is of a general nature and is not intended to address the circumstances of any particular individual or entity. Although we endeavor to provide accurate and timely information, there can be no guarantee that such information is accurate as of the date it is received or that it will continue to be accurate in the future. No one should act on such information without appropriate professional advice after a thorough examination of the particular situation.

Legal services may not be offered to SEC registrant audit clients or where otherwise prohibited by law.

© 2020 KPMG Tax and Advisory LLC, a company incorporated under the Laws of the Republic of Kazakhstan, a member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved.

The KPMG name and logo are registered trademarks or trademarks of KPMG International.