

# KAZAKHSTAN

## TRADE SUMMARY

The U.S. goods trade deficit with Kazakhstan was \$315 million in 2006, a decrease of \$248 million from \$563 million in 2005. U.S. goods exports in 2006 were \$646 million, up 20.0 percent from the previous year. Corresponding U.S. imports from Kazakhstan were \$961 million, down 12.8 percent. Kazakhstan is currently the 75<sup>th</sup> largest export market for U.S. goods.

The stock of U.S. foreign direct investment (FDI) in Kazakhstan in 2005 was \$3.9 billion (latest data available), down from \$4.7 billion in 2004.

Kazakhstan has been negotiating membership in the WTO since January 29, 1996. Kazakhstan is still negotiating bilateral agreements with a number of WTO Members, including the United States, the European Union and Australia. In 2006, Kazakhstan signed protocols with Honduras, Dominican Republic, Bulgaria and Norway. Currently, 14 countries out of 39 members of the Working Party for Kazakhstan have signed bilateral protocols. While progress has been made in 2006 in implementing WTO-consistent legislation, more work remains in a number of areas, including reforming customs practices, Sanitary and Phytosanitary (SPS) regulation, Technical Barriers to Trade (TBT), government procurement, and taxation.

The United States-Kazakhstan Bilateral Trade Agreement, which came into force in 1993, grants reciprocal, normal trade relations treatment. A bilateral investment treaty (BIT) came into force in January 1994.

## IMPORT POLICIES

Kazakhstan is a member of the Eurasian Economic Community (EAEC), along with Russia, Kyrgyzstan, Belarus, Tajikistan and Uzbekistan. Armenia, Moldova and Ukraine currently have observer status. In 2006, Kazakhstan, Russia, and Belarus announced the formation of a trilateral customs union. There are plans to bring the customs union into force in 2007 and to eventually expand it to include other EAEC countries. The customs union aims to bring about coordinated customs procedures and a high degree of uniformity in its members' external tariffs.

The weighted-average applied import tariff in Kazakhstan is approximately 7.5 percent. Goods imported for short-term use in Kazakhstan under a temporary import regime can be fully or partially exempt from duties, taxes and non-tariff regulations. The government has the right to issue a list of goods that cannot be temporarily imported into Kazakhstan. Typical examples of articles not eligible for duty exemptions are food products, industrial waste, and consumables.

The Law on Investments, enacted in January 2003, provides customs duty exemptions for imported equipment and spare parts, but only if Kazakhstan-produced stocks are unavailable or not up to international standards. Kazakhstan's new Customs Code became effective on May 1, 2003, superseding the previous law which had been in effect since 1995. There are positive changes in the Code, such as provision for WTO-compliant customs valuation methodologies. In practice, however, customs administration remains a problematic aspect of trade. In addition, key provisions for such practices as voluntary disclosure are not included in the Code.

## FOREIGN TRADE BARRIERS

U.S. exporters to Kazakhstan have consistently identified the requirement to obtain a "transaction passport" to clear imported goods through customs as a significant barrier to trade. This regulation is designed to stem capital outflows and money laundering by requiring importers to show copies of contracts and other documentation to legitimize and verify the pricing of import/export transactions. The practice retards the growth of trade, as the regulations place relatively tight restrictions on transaction parameters. For example, the regulations allow a maximum financing term for imports of 120 days, after which time the transaction passport lapses; extending it requires the approval of the National Bank. This requirement limits the range of business activity and creates a potential bias toward short-term financing in the economy.

There is a simplified customs regime for small entrepreneurs and individuals carrying cargo valued up to \$10,000. This provision favors "shuttle" traders bringing in goods from neighboring countries and may contribute to Kazakhstan's "shadow economy." Amendments to the Customs Code, aimed at bringing Kazakhstani legislation further into compliance with the WTO standards, are currently in the works. Among the proposed changes is the simplification of the transaction passport requirement. The government hopes to enact the new statutes in 2007.

## **STANDARDS, TESTING, LABELING AND CERTIFICATION**

Between 2004 and 2006, the Kazakhstani government adopted the following laws in furtherance of its efforts to develop a national system of standardization and certification: "On Technical Regulation"; "On Ensuring Uniformity of Measurement;" "On Supporting Government Regulations;" and "On the Mandatory Confirmation of Compliance of Products in the Republic of Kazakhstan."

The Kazakhstani Law on Technical Regulation distinguishes the state's responsibilities from those of the private sector. The government is responsible for product safety but delegates quality control responsibilities to authorized private institutions. A wide range of goods are subject to mandatory certification requirements which apply to both domestically-produced and imported goods. A related regulation lists the specific categories of products subject to certification, including machines, cars, agricultural and telecommunications equipment, construction materials, fuel, clothes, toys, food and drugs.

Standards for imported goods are addressed further in the Law on Technical Regulation which specifies that contracts for the delivery of imported goods subject to mandatory certification should be required to confirm compliance with Kazakhstani mandatory certification requirements. Delivery contracts must also be accompanied by documents describing the products and listing the country of origin, the producer, the expiration date, any storage requirements as well as the code of use in both the Kazakh and Russian languages. In addition, the law states that foreign certificates, testing protocols and compliance indicators must be in accordance with international treaties.

In lieu of requiring re-labeling of imported products, the Kazakhstani government accepts the addition of Kazakh language stickers on those products. Kazakhstan has also issued a wide-ranging regulation exempting pharmaceutical products and several other categories of goods from the Kazakh labeling requirement.

Kazakhstan intends to accede to the International Laboratory Accreditation Conference (ILAC) and the International Accreditation Forum (IAF). This step would automatically make Kazakhstan a party to a number of international treaties on metrology and standards.

## **FOREIGN TRADE BARRIERS**

The government has opened an Information Center to provide information on technical regulations to foreign companies and governments. A variety of information, including information on technical regulations, is available on the Information Center's website, but only in Russian and Kazakh.

New legislation aimed at bringing the legal environment into compliance with the WTO Agreement on Technical Barriers to Trade is in the course of being developed. New draft laws and amendments, such as statutes dealing with product safety, are being considered by the Parliament.

## **GOVERNMENT PROCUREMENT**

Kazakhstan is reforming and harmonizing its system of state procurement. Some potential U.S. suppliers have raised concerns about the transparency and efficiency of Kazakhstan's government tender process. The "Regulation on the State Procurement Agency" was approved in March 1999. In October 2004, the State Procurement Agency was merged with the Committee on Financial Control and subordinated to the Ministry of Finance. The procurement process in Kazakhstan is regulated by the law "On State Procurement" and by the Budget Code.

The government has taken steps to improve the transparency of the procurement process. In particular, the Committee on Financial Control has published on its website the list of agencies and state enterprises that are subject to state procurement regulations (the "Rules of Inclusion and Exclusion") and a blacklist of unfair and unreliable suppliers of goods and services. However, the government procurement situation remains problematic. Further legislative improvement in this area is needed. The government is currently developing new procurement legislation, which it hopes to adopt in 2007.

The "Rules on Oil and Gas Procurement" give significant preferences to local suppliers, and establish what many firms, foreign and domestic, consider unwarranted state interference in even small tenders.

## **INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION**

The government's effort to diversify the economy away from the energy sector and spur the growth of a domestic high technology industry, along with the WTO accession process, has led to a strong emphasis on IPR protection. The progress achieved on the legislative front as well as in enforcement was reflected in the May 2006 removal of Kazakhstan from the USTR's Special 301 Watchlist. Although pirated films and music are still widely available, the vast majority are believed to be imported, not produced domestically. Armed with November 2005 statutes authorizing stiffer penalties for violators, the authorities have conducted numerous raids against distributors of pirated recordings.

The government's efforts have greatly helped to expand the Kazakhstani market for licensed goods. Still, much remains to be done, particularly in making the customs controls a more effective line of defense against incoming infringing goods. Legislation granting customs officials *ex officio* powers is reportedly under development. Further progress is also needed in the realm of civil adjudication, where an increasing number of IPR disputes are being settled. Although civil courts have been used effectively to stem IPR infringement, judges often lack expertise in the area of IPR.

## **SERVICES BARRIERS**

The Oil and Gas Procurement Regulations stipulate that oil companies must purchase services only from Kazakhstan-based companies unless the required service is unavailable in Kazakhstan.

## **FOREIGN TRADE BARRIERS**

Concerns have been raised about possible preferential treatment for Kazakhstan's recently launched domestic satellite (KazSat 1), which could result in competitive disadvantages for U.S. satellite operators serving the Kazakhstan market.

## **INVESTMENT BARRIERS**

Kazakhstan's 2003 Law on Investments provides the legal basis for foreign investment in Kazakhstan. In general, investors have concerns about the law's narrow definition of investment disputes, its lack of clear provisions for access to international arbitration, and certain aspects of investment contract stability guarantees.

Most foreign investment in Kazakhstan is attracted to the oil and gas sector. One notable aspect of this sector is the State's active promotion of "local content" in purchases of goods and services for petroleum operations. (Such requirements may raise concerns with respect to the performance requirements obligation of the United States-Kazakhstan Bilateral Investment Treaty (BIT), which entered into force in 1994.) For example, the 1999 amendments to the Oil and Gas Law required mining and oil companies to favor local goods and services. The rules implementing these legal provisions were enacted in June 2002 (Decree 612). The decree has had an onerous effect on investors by also requiring government involvement in, and approval at, each stage of private procurement.

Amendments to the Law on Subsurface Use, adopted in December 2004, require investors to state in their tender proposals what affirmative actions they will take to satisfy local content requirements. Operations can be suspended for up to six months if a company is found to have failed consistently to meet the requirements.

In addition, the July 2005 Law on Production-Sharing Agreements (PSAs) contains explicit requirements regarding the local purchase of goods and services and the hiring of Kazakh nationals, and applies to all investment in offshore oil and gas exploration and production. The new law also requires that KazMunayGas, the national oil company, have a minimum 50 percent share in offshore projects, and it creates a new means by which the national oil company may obtain field rights outside of a tender process. Taken together, these clauses establish KazMunayGas as a necessary partner for international oil companies investing offshore, at least in the initial stages of an agreement.

In 2005, Kazakhstan added a controversial "pre-emption" amendment to its Law on Subsurface Use. The amendment guarantees the state the right of first refusal when a party seeks to sell any part of its stake in a mineral resource extraction project. The state claims this preeminent right even in cases where the controlling agreement assigns pre-emptive rights elsewhere (*e.g.*, to other investors in a consortium). The amendment applies the pre-eminent right retroactively. This amendment raises serious questions about the government's respect for contract sanctity.

In October 2005, the government asserted even broader pre-emption rights under national law by claiming for itself pre-emptive rights when an investor seeks to purchase a company that possesses drilling rights. Theoretically, this latest assertion of pre-emptive rights (which has not yet been tested in court) could be read as a statement that the government of Kazakhstan has a preferential right to purchase or prevent the sale of stock in any company that is involved in the oil, gas or mining sectors in Kazakhstan.

The Law on Subsurface Use prohibits gas flaring except in emergency cases. Amendments adopted in October 2005 mitigated this requirement, providing for a transition period up to July 1, 2006, for subsurface users to draft and present to the government a program for gas utilization.

## **FOREIGN TRADE BARRIERS**

Kazakhstani law allows citizens of Kazakhstan and foreigners to own land under commercial and non-commercial buildings, including dwellings and associated land. Such land may also be leased for up to 49 years. The new land code, which came into effect in June 2003, for the first time allowed the private ownership by Kazakhstanis of agricultural land, in addition to industrial, commercial, and residential land. Foreign individuals and companies may still only lease agricultural land for up to 10 years, however, and the wording of the law is unclear with regard to the purchase of such land by local legal entities, either wholly-owned or joint ventures. Kazakhstani authorities often require, as part of a foreign firm's contract with the government, that the firm contribute to social programs for local communities.

Foreign ownership of individual mass media companies is limited to 20 percent. Foreign insurance companies are limited to operating in Kazakhstan through joint ventures with Kazakhstani companies. Overall capital of all foreign insurance companies may not exceed 25 percent of the non-life insurance market and 50 percent of the life insurance market. Legislation that lifted the restrictions on foreign participation in the registered capital of Kazakhstani banks was approved and came into force in December 2005. However, some restrictions on non-residents' activity in the financial sector still remain. Limitations on foreign ownership in the banking and insurance sectors may raise concerns with respect to the national treatment obligation of the United States-Kazakhstan BIT.

Foreign investors continue to have difficulty obtaining work permits for employees who are not Kazakhstani nationals. The quota is set each year, based on a percentage of foreign labor as a share of the total national work force. Many companies report that permits for key managers and technicians are routinely rejected or granted for unreasonably short periods or are conditioned upon demands for additional local hires. Companies also note that hiring regulations are confusing and interpreted inconsistently by local officials and by the Ministry of Labor and Social Protection.

The government, however, has been steadily increasing the number of work permits available. In 2004, the number of permits was limited to 0.21 percent of the economically active population (estimated at about 8 million people). The figure increased to 0.32 percent in 2005 and to 0.55 percent in 2006. For 2006, the quota for the first and second categories (managers and professionals) was increased from 0.21 percent to 0.24 percent. For the third category (skilled workers), the quota rose from 0.11 percent to 0.18 percent. For the fourth category (seasonal farm workers), the quota remains unchanged at 0.13 percent.

Kazakhstan adopted a new international commercial arbitration law in late 2004. The law defines the role for international arbitration institutions in Kazakhstan at all stages, from the adoption of an arbitration clause in a contract through the execution of an arbitral decision. The law defines the organizational and legal elements of arbitral proceedings in Kazakhstan, and the conditions for recognition and execution of arbitral decisions made in foreign states. In practice, the government of Kazakhstan has not consistently observed international practices relating to the enforcement and recognition of arbitral awards.

## **OTHER BARRIERS**

There are other structural barriers to investment in Kazakhstan, including a weak system of business law, a lack of an effective judicial system for breach-of-contract resolution and an unwieldy government bureaucracy. Many companies serving the Kazakhstani market report significant logistical difficulties. In addition, there is a burdensome tax monitoring system for all companies operating in Kazakhstan. Many companies report the need to maintain excessively large staffs in Kazakhstan to deal with the cumbersome tax system and frequent inspections. The tax authorities have, on occasion, initiated criminal cases against local employees of foreign firms.

## **FOREIGN TRADE BARRIERS**