



## MAJOR KAZAKHSTAN LEGISLATION CHANGES FOR 2017

GRATA Finance & Securities Group Legal Alert



In keeping with GRATA's practice of informing clients regarding important legal developments that might influence their business, allow us to draw your attention to the following changes in Kazakhstani legislation that occurred during 2017



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Shaimerden Chikanayev  
Partner, Finance & Securities Group  
M. +7 701 787 80 20  
E. schikanayev@gratanet.com



Marina Kahiani  
Partner, Finance & Securities Group  
M. +7 701 725 1269  
E. mkahiani@gratanet.com



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## KAZAKHSTAN IN 2017 AT A GLANCE

2017 has been a big year for Kazakhstan: it hosted an international expo in Astana and held a non-permanent seat on the United Nations Security Council and replaced Geneva as host to Syrian peace talks. As far as the overall economy is concerned, Kazakhstan in 2017 suffered badly from the 2014 price decline in oil and other commodities and a stagnant banking sector. As such, its future economic growth largely depends on attracting foreign direct investment (FDI) flow into Kazakhstan for the development of infrastructure and regional trade. Kazakhstan aims to become the largest business and transit hub in the Central Asia region, bridging Europe and Asia. To meet this goal, the legal and regulatory framework of Kazakhstan has undergone a series of reforms in 2017, in the hope of moving away from the oil and gas industry as its main source of income that ultimately shall help to attract new foreign finance institutions and give Kazakhstan a unique competitive advantage in attracting foreign direct investments and help the country achieve its goal of becoming a leading financial center for the region.



## AMENDMENTS AIMED ON IMPROVEMENT OF BUSINESS CONDITIONS

The Law on Amendments Intended to Improve Business Conditions<sup>1</sup> (the “**Business Improvement Law**”) came into effect on 12 March 2017, except certain provisions.

The purpose of the Business Improvement Law is to further improve the investment climate in line with the general policy of the country to support local entrepreneurs and foreign investors.

The Business Improvement Law amends 7 codes and 38 laws of the Republic of Kazakhstan.

### *Legal Division of Invalid Transactions into Voidable and Void*

One of the main changes introduced by the Business Improvement Law is the division of invalid transactions into voidable and void (Article 157 of the Civil Code<sup>2</sup>). Before, such division existed only in legal doctrine and not in the legislation. The difference between voidable and void transactions is that, in order to be held invalid, voidable transaction shall be challenged in court, whereas void transaction is invalid *ab initio* by the virtue of law and without any court decision.

The change is intended to decrease the number of disputes in relation to void transaction (since it will now be obvious to the parties that the transaction is void/invalid *ab initio* by the virtue of law and that there is no sense in challenging it in the court). However, if one of the parties disagrees that the transaction is void, it can still apply to the court (though the perspective of such cases would be low).

The Business Improvement Law clarified that void transactions include, *inter alia*, transactions that have not been notarised/concluded in written form where such notarisation/written form was required by law (Article 153.2, 154.1 of the Civil Code).

### *Decrease of Amount of Penalties by Court*

Previously, a Kazakh court at its own discretion could decrease the amount of penalties indicated in the contract or requested by the party. Following adoption of the Business Improvement Law, such decrease is possible only upon relevant request of a debtor (Article 297 of the Civil Code).

### *Simplification of Requirements Applicable to Pledge Agreements*

Article 307 of the Civil Code establishes mandatory provisions of a pledge agreement. Absence of such provisions in a pledge agreement makes it void.

The Business Improvement Law simplified such mandatory provisions. Firstly, value of the pledged property shall now be indicated only in relation to the pledge of immovable property (before, it was mandatory for the pledges of both immovable and movable property). Secondly, the Business Improvement Law abolished the mandatory requirement to indicate the value of

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<sup>1</sup>Law of the Republic of Kazakhstan dated 27 February 2017 No. 49-VI “On Introduction of Amendments and Additions to Some Legislative Acts of the Republic of Kazakhstan on Issues of Improvement of Civil, Banking Legislation and Improvement of Conditions for Entrepreneurial Activity”

<sup>2</sup> Civil Code (General Part) of the Republic of Kazakhstan dated 27 December 1994

pledged property in 2 currencies – KZT and currency of the secured obligation (Article 307 of the Civil Code).

These amendments are intended to remove unnecessary requirements and to make pledging property easier. For example, the previously mandatorily required value of pledged movable property did not make a lot of sense since it could be established as any figure at discretion of the parties and was not useful for any purpose.

#### *Amendment of Rules Applicable to Pledge of Goods in Circulation*

Previously, the agreement for pledge of goods in circulation had to mandatorily provide for the minimal value of pledged goods (i.e. the total value of the pledged goods in circulation could not be less than this minimum at all times). Now, such minimal value of the pledged goods can be established by parties at their discretion (Article 327 of the Civil Code).

#### *Obligation of Pledgee to Terminate Pledge of Movable Property in 1 Day*

The Business Improvement Law introduced the requirement for a pledgee under movable pledge agreement to file the application for termination of the pledge to the relevant registration body within 1 business day upon performance of the secured obligations (Article 10 of the Law on Registration of Pledges of Movable Property<sup>3</sup>). There is no similar obligation for a pledgee under pledge of immovable property.

This novelty seems to create practical difficulties, especially for foreign pledgees who might not be able to deliver the application from abroad within 1 day upon the moment of the secured obligations performance.

#### *Obligation of Individual Entrepreneur to Conclude Public Agreements*

A public agreement is an agreement stipulating the obligations of an entrepreneur to sell goods, carry out works or render services which such an entrepreneur shall provide for in relation to any potential customer due to the character of its business activity (e.g. transport services, electricity etc). As a general rule, the conditions of a public agreement shall be equal to all customers and an entrepreneur cannot prefer one customer over another in the conclusion of public agreements.

Previously, the above obligation applied to commercial legal entities only, now it also applies to individual entrepreneurs (Article 387 of the Civil Code).

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<sup>3</sup> The Law of the Republic of Kazakhstan dated 30 June 1998 No. 254-I “On Registration of Movable Property Pledge”

*Amendments to the Banking Law<sup>4</sup>*

The Banking Law regulates so called “bank holdings”<sup>5</sup> and “major participants”<sup>6</sup> of Kazakh banks. The activity of these persons is limited to transactions expressly permitted by the Banking Law and they are subject to stringent prudential requirements established by the National Bank of Kazakhstan (the “NBK”).

The Business Improvement Law made an exemption from above regulation for organisations specializing in improving quality of loan portfolios of Kazakh banks<sup>7</sup> and subsidiaries of the NBK (Article 2.4), Article 2.6) of the Banking Law). Accordingly, these entities are not subject to “bank holdings” and “major participants” regulation, even if they actually own a relevant number of a Kazakh bank’s shares (25% or more/10% or more).

Further, the Business Improvement Law removed the restriction on organisations specializing in improving quality of loan portfolios of Kazakh banks to deal only with bad assets of the bank. Now, for example, such an organisation can acquire non-problem assets of Kazakh banks and will be able to become a shareholder of a non-problem Kazakh bank, which was prohibited before (Article 5-1.2, Article 17.2 of the Banking Law).

The Business Improvement Law clarified that in case of transfer of a bank’s assets to an organisation, no consent of any party (debtor, guarantor etc.) is required (Article 5-1.2.11 of the Banking Law).

Further, a special favourable regime of voluntary banks reorganisation (presumably, in form of a merger of one bank with another<sup>8</sup>) that used to apply only to the reorganisation of restructured banks, will now also apply to the reorganisation of other (not restructured) banks (Article 60-1 of the Banking Law).

The special operation for simultaneous transfer of assets from a subsidiary bank to a parent bank, designed to save problem banks, will now apply to any subsidiary and parent bank, not only to restructured subsidiary and parent bank (Article 61-4 of the Banking Law).

We understand that such measures have been introduced to provide more options for the recovery of the Kazakh banking sector, which is experiencing difficulties with the quality of loans.

*Introduction of a Statute of Limitation to the Borrowers under Non-Performing and (or) Improper Performing Bank Loans*

The Business Improvement Law introduced a 5-year statute of limitation in relation to claims of banks and other banking activity related organisations on borrowers under non-performing and (or) improper performing bank loan agreements (Article 37 of the Banking Law). Prior to this amendment there was no statute of limitation in relation to bank loans.

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<sup>4</sup>The Law of the Republic of Kazakhstan dated 31 August 1995 No. 2444 “On Banks and Banking Activity in the Republic of Kazakhstan”

<sup>5</sup>Broadly, a person or a group of persons with 25% or more shareholding

<sup>6</sup>Broadly, a person or a group of persons with 10% or more shareholding

<sup>7</sup> An organisation 100% owned by the Kazakh Government whose main activity is to acquire Kazakh banks’ assets in order to improve their financial position (Article 5-1.1 of the Banking Law)

<sup>8</sup> It is not clear from the Banking Law whether such regime applies to reorganisation generally or only to merger of one bank to another

### *Introduction of Mandatory Audit of Annual Financial Statements for LLPs*

Under the Business Improvement Law, audit of the annual financial statements is mandatory for an LLP if the following conditions are met simultaneously (Article 59 of the Law on Partnerships<sup>9</sup>):

- 1) LLP has participants (founders) owning less than 10% participatory interests in the charter capital;
- 2) the average annual number of employees is more than 250 people and (or) the average annual income is over a 3 million-fold of monthly calculation index<sup>10</sup>.

Audit of the annual financial statements of a LLP being a medium-sized business entity<sup>11</sup>, shall be mandatorily carried out per request of a participant (founder) owning less than 10% participatory interests in the charter capital.

### *Taking Decision on Placement of Shares of Public JSC*

The Business Improvement Law clarified that the decision on the placement of shares of a public joint stock company<sup>12</sup>, within the number of announced shares, shall be taken by the general meeting of shareholders (Article 18 of the JSC Law<sup>13</sup>). Such a decision in relation to a “non-public” company still refers to the exclusive jurisdiction of the Board of Directors (Article 53.2.3) of the JSC Law).

### *Additional Disclosure Requirements*

Now, a JSC shall inform its shareholders and investors about entering into an interested party transaction, when a JSC acquired or alienated a property-which value constitutes 10% or more of the total amount of the balance value of its assets (Article 79.1 of the JSC Law).

Now, a legal entity that has purchased more than 20% of the voting shares of JSC-shall, within 30 calendar days from the moment of acquisition, publish information on these shares owned by such a legal entity in the mass media, as determined by the charter of JSC (Article 95.5 of the Civil Code, Article 25.5 of the JSC Law).

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<sup>9</sup> The Law of the Republic of Kazakhstan dated 22 April 1998 No. 220-I “On Partnerships with Limited and Additional Liability”

<sup>10</sup> Monthly calculation index is an indicator established annually for the purposes of calculation of monthly average salaries, pensions, social payments, fines etc. In 2018, monthly calculation index is KZT 2,405 or approximately USD 8

<sup>11</sup> Medium-sized business entity is an entity with annual average number of employees of 101-250 and/or annual average income of 300 – 3,000,000 monthly calculation indexes (Article 24 of the Business Code)

<sup>12</sup> A joint stock company is a public joint stock company if it meets each of the following criteria: (a) its shares are available for purchase for an unlimited range of investors in the non-organised and/or organised securities market; (b) not less than 30% of the total amount of the placed common shares belong to shareholders, each of which owns not more than 5% of the common shares out of the total number of the placed common shares; (c) the volume of trades with common shares of the joint stock company satisfy the requirements established by the NBK; and (d) the shares of the joint stock company are included on the list of stock exchange, operating in Kazakhstan (i.e., listed on KASE or AIX) (Article 4-1 of the JSC Law).

<sup>13</sup> The Law of the Republic of Kazakhstan dated 13 May 2003 No. 415-II “On Joint Stock Companies”

*Introduction of a New Ground for Invalidation of a Transaction of JSC*

The Business Improvement Law introduced a new ground of invalidation of an interested party transaction, when a JSC acquired or alienated a property-which value constitutes 10% or more of the total amount of the balance value of its assets.

If such a transaction caused damage to a JSC, the transaction may be invalidated by court at request of the JSC itself or its shareholder(s) owning (jointly) 5% or more of voting shares if:

- it is proven that as of the moment of taking the decision on such a transaction, the value of the relevant property significantly differed from its market value indicated by an independent appraiser; and
- a court establishes that the shareholders of the JSC were deliberately deceived by an official(s) of the JSC to get profit for himself (themselves) or his affiliates (Article 74.1 of the JSC Law).

The above can also be a ground for bringing a relevant official of the JSC to liability (Article 63.1-1 of the JSC Law).

*Consequences of Invalidation of a Transaction Concluded on Organised Securities Market*

The Business Improvement Law introduced quite a controversial amendment to the Securities Market Law<sup>14</sup>.

Now, if a transaction concluded on organised securities market is held invalid, the restitution (the arrangement where the parties shall reinstate the initial position, i.e. return each other everything they received as a result of transaction) shall NOT apply (unlike in case of any other invalidated transaction).

Instead, the party which is guilty of committing actions that caused the invalidity of the transaction, shall compensate the losses of the party or person whose rights and legitimate interests were violated as a result of the transaction (Article 88.4 of the Securities Market Law).

The amendment was obviously intended to provide assurance in securities ownership for organised market participants, however, such an approach may cause a problem in a situation where, for example, a guilty party does possess the securities received as a result of transaction, however, not the cash to compensate the losses.

*Amendments to the List of Bonds Allowed for Purchase by Banks and Bank Holdings*

As mentioned above, according to the Banking Law, banks and bank holdings are generally prohibited from any non-banking business activity and transactions with securities except those specifically permitted by the Banking Law.

One of the prohibitions is a prohibition to banks and bank holdings to purchase bonds, except bonds issued by international financial organisations designated by the NBK and bonds that meet certain criteria established by the NBK.

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<sup>14</sup>The Law of the Republic of Kazakhstan dated 2 July 2003 No. 461-II “On Securities Market”

Previously, though the Banking Law referred to the list of international financial organisations designated by the NBK, the bonds issued by which can be purchased by Kazakh banks and bank holdings, there was actually no such a list.

Resolution of the Management Board of the NBK No. 234 dated 29 November 2017 (the “**Resolution 234**”) corrected this discrepancy by establishing the list of such international financial organisations, including the Islamic Corporation for the Development of the Private Sector, the Asian Development Bank, the European Bank for Reconstruction and Development, the International Finance Corporation, the Eurasian Development Bank and others.

The Resolution 234 also extends the list of bonds which banks and bank holdings are allowed to purchase, the following items have been added:

- (i) bonds that have the status of state securities of Kazakhstan (including those which were issued in accordance with the legislation of other states) issued by the Ministry of Finance of the Republic of Kazakhstan or by the NBK;
- (ii) bonds issued by the local executive bodies of Kazakhstan that are included in the official list of the stock exchange, which carries out activities in the territory of Kazakhstan (i.e. KASE or AIX);
- (iii) bonds issued by Kazakh entities which are included in the official list of the stock exchange, which carries out activities in the territory of Kazakhstan (i.e., KASE or AIX), except the bonds that are in the “buffer category” of the “debt securities” sector of the official list of the stock exchange.

The Resolution 234 clarifies that “allowed for purchase” bonds that have the status of government securities of the foreign countries shall be issued by the central governments of such foreign countries.

## **AMENDMENTS IN THE SPHERE OF INVESTMENTS**

The Law No.122-VI<sup>15</sup> amended various laws, including the Commercial Code<sup>16</sup> in the part of foreign investments regulation. The most important changes are listed below.

### *Deadline for Auditors Report*

The Law No.122-VI introduced 2-month deadline for the submission of audit report confirming performance of investment obligations to the Ministry for Investments and Development by the legal entity of the Republic of Kazakhstan which concluded the investment contract. Such deadline did not exist before.

In addition, now if the investment contract provided for the investment subsidy, the auditor’s organisation that checked performance of investment obligations under such contract, shall meet minimal criteria established by authorised body in the sphere of audit (Article 159.7 of the Commercial Code).

### *Abolishment of Requirement to Establish New Legal Entity in Kazakhstan*

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<sup>15</sup> The Law of the Republic of Kazakhstan No 122-VI dated 25 December 2017 “On Amendments and Additions to Some Legal Acts of the Republic of Kazakhstan on Tax Issues” (the “**Law 122-VI**”)

<sup>16</sup> Commercial Code of the Republic of Kazakhstan dated 29 October 2015 No. 375-V

The Commercial Code was amended by the abolishment of requirement to establish a new legal entity of the Republic of Kazakhstan in order to receive investment preferences. Now, the existing Kazakh legal entity can enter into the investment contract and receive investment preferences.

#### *Changes to the Criteria of Investment Priority Projects*

The Law No.122-VI amended the definition of “investment priority project”. Previously, the investment project was considered as “investment priority project” if such project was implemented in relation to the activity included to the list of priority activities established by the Government and the amount of such investment project was a 2 million-fold of monthly calculation index (approximately 16 million USD). Now, the Commercial Code requires the amount of the investment priority project to be: 2 million-fold of monthly calculation index (approximately 16 million USD) if the project relates to construction of the new production facilities and 5-million fold of monthly calculation index (approximately 40 million USD) if the project relates to the improvement and renewal of the existing production facilities (Article 284 of the Commercial Code).

Previously, the Commercial Code prohibited to use budget funds for the purposes of implementation of investment priority project. Now it is allowed provided that such budget funds are provided in a form of lease finance, a loan or other repayable type of finance (Article 286.5.6) of the Commercial Code)

#### *Additional Preferences for Special Investment Projects*

For the special investment projects<sup>17</sup>, the Government will now provide not only custom preferences, but also tax preferences – now import of raw and other materials for the purposes of special investment project is free of VAT (Article 283.5, 290.2.3) of the Commercial Code).

#### *Abolishment of Preferences for Investment Strategic Projects*

The preferences for investment strategic projects have been abolished and definition of “investment strategic project” has been removed from the Commercial Code. Now, investment preferences can be obtained in relation to investment project, investment special project and investment priority project (Article 284 of the Commercial Code).

#### *Changes Related to Provision of Investment Subsidy*

Investment subsidy is one of the types of non-repayable investment preferences provided to the legal entity of the Republic of Kazakhstan that concluded investment contract for realisation of investment priority project.

After the amendments introduced by the Law No.122-VI, investment subsidy can be only provided in relation to the investment priority project for the amount of not less than 5-million fold of monthly calculation index approximately, 40 million USD (Article 291.1 of the

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<sup>17</sup> Special investment project is an investment project realised by the legal entity of the Republic of Kazakhstan, registered as a participant of special economic zone or owner of free warehouse as provided by customs legislation of the Republic of Kazakhstan, or the project, realised by a legal entity of the Republic of Kazakhstan that entered into agreement on industrial assembly of motor transport vehicles (Article 284 of the Commercial Code)

Commercial Code). Previously it could be provided in relation to any investment priority project without limitation of the amount of investments. In addition, investment subsidy can now only be provided in relation to the new production facilities and not in relation to improvement and renovation of the existing production facilities (Article 283.3 of the Commercial Code).

Investment subsidy can now only be provided in relation to the investment priority projects in certain spheres eligible for the provision of investment subsidy, the list is established by the Government (Article 291.2 of the Commercial Code).

The Law No.122-VI provided for the full return of the investment subsidy in case of termination of the investment contract (Article 295.6-1 of the Commercial Code).

## **AMENDMENTS IN THE SHPERE OF ELECTRIC POWER INDUSTRY**

The Law 89-VI<sup>18</sup> came into effect on 24 July 2017, except certain provisions.

The purpose of the Law 89-VI is to improve reliability of energy supply, address issue of ownerless electric network and increase attractiveness of renewable energy projects.

The Law 89-VI amends 4 codes and 7 laws of the Republic of Kazakhstan. The most important amendments are described below.

### *Granting of Ownerless Electric Network to Energy Transmission Companies*

The Law 89-VI addressed the issue of ownerless electric network that existed in Kazakhstan for quite a while. Nobody was responsible for the ownerless electric network that caused uncertainty and challenges for the whole electric system. Following adoption of the Law 89-VI, electric network recognised as ownerless shall be granted by the local executive bodies (Akimats) to the energy transmission organisations to which such ownerless electric network is connected (Article 119-2 of the Law on State Property<sup>19</sup>).

### *Transfer of Electric Network to Energy Transmission Companies*

The owner of electric network that renders services on transmission of electric energy, is now entitled to sell, transfer on a free of charge basis or for the trust management its electric network to an energy transmission organisation to which its electric network is connected (Article 13-1.1 of the Electric Power Industry Law<sup>20</sup>).

State legal entities operating electric network on the basis of right of economic management or operational management, are obliged to transfer it to the trust management or uncompensated use of energy transmission organisations to which electric network is connected. Such transfer shall be completed by 1 January 2019 (Articles 13-1.1.2, 25.7 of the Electric Power Industry Law).

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<sup>18</sup>Law of the Republic of Kazakhstan dated 11 July 2017 no. 89-VI “On Introduction of Amendments and Additions to Some Legislative Acts of the Republic of Kazakhstan on Issues of Electric Power Industry”

<sup>19</sup> The Law of the Republic of Kazakhstan dated 1 March 2011 No. 413-IV “On State Property”

<sup>20</sup> The Law of the Republic of Kazakhstan dated 9 July 2004 No. 588-II “On Electroenergy”

*Introduction of Requirements to Energy Transmission Organisations*

The Law 89-VI introduced requirements which shall be met by both new and existing energy transmission organisations by the certain deadlines (Articles 13-1.6, 13-1.7, 25.6 of the Electric Power Industry Law):

- ✓ availability of dispatching technological management – by 1 January 2018;
- ✓ special divisions responsible for operation and technical support of electric network, equipment, mechanism, labour protection and safety measures – by 1 January 2020;
- ✓ agreements with system operator – by 1 January 2020;
- ✓ automated systems of commercial records, systems of telecommunications ensuring their unification with systems of system operator and regional electric grid company – by 1 January 2022.

Expenses associated with meeting the requirements shall not be included in calculation of tariffs, i.e. will not be recovered by energy transmission companies.

*Establishment of Specific Tariffs for Transmission of Electric Energy*

In case of transfer of electric network to a subject of natural monopoly, the tariffs for electric energy transmission or tariff estimate for such subject of natural monopoly can be reconsidered by the Committee on Regulation of Natural Monopolies, Protection of Competition and Rights of Consumers of the Ministry of National Economy of the Republic of Kazakhstan (the “**Antimonopoly Body**”) (Article 18.3, 14.1.17-3 of the NML).

If a subject of natural monopoly rendering services on transmission of electric energy does not meet the requirements for energy transmission organisations established by the Electric Power Industry Law, its tariff or maximum level of tariff is subject to adjustment by the Antimonopoly Body. The adjustment is made by exclusion of investment and other expenditures of the subject of natural monopoly from the tariff (Article 18.8 of the NML). This measure is aimed to encourage energy transmission organisations to meet the requirements established by the Electric Power Industry Law.

*Subsidising Purchase of Fuel by Energy Producing Organisations*

The Law 89-VI introduced state subsidies to be provided to energy producing organisations for the purchase of fuel in order to avoid any interruptions during the heating season. Such subsidies shall be provided by the local executive bodies of oblasts, Almaty and Astana (Akimats) according to the rules established by the Ministry of Energy of the Republic of Kazakhstan (Articles 5.70-30, 5-2 of the Electric Power Industry Law).

*Differentiation of Tariffs on Electric Energy*

The Law 89-VI abolished differentiation of tariffs on electric energy depending on time zone (Articles 1.31, 7.1 of the Electric Power Industry Law).

Maximum term for approval of maximum tariffs for a group of energy producing organisations is reduced from seven (7) to three (3) years (Article 12-1.2 of the Electric Power Industry Law).

*Template Agreements for Energy Supply Organisations*

Energy supply organisations shall enter into agreements with consumers on basis of template agreements differentiated for three (3) categories of consumers: residential consumers, consumers using electric energy not for residential purposes and legal entities financed from the state budget. Template agreements shall be published on web-sites of energy supply organisations (Articles 18.1-1, 13.3 of the Electric Power Industry Law).

*Establishment of Conditions for Export and Import of Electric Energy from and to Kazakhstan*

Following adoption of the Law 89-VI, export of electric energy from Kazakhstan is possible only in case of proficit of electric energy in Kazakhstan. Similarly, import to Kazakhstan is allowed only in case of deficit of electric energy in Kazakhstan. Both proficit and deficit shall be approved by the system operator. Export shall be made for the price not less than cost of production of electric energy. The only possible exclusions from these rules are sale-purchase of electric energy by the system operator to ensure agreed amounts of electric energy flow, to provide emergency mutual aid to the energy systems of neighbouring countries and at balancing market of electric energy (Articles 5.70-29, 10.1.22-2, 13.9-13.11 of the Electric Power Industry Law). Balancing market is established among the system operator and energy producing, energy transmission, energy supply organisations, wholesale consumers in case of imbalances between agreed and factual amounts of production and (or) consumption of electric energy in current operational day in Kazakhstan.

Position of national operator, which was authorised for centralised export and import of electric energy before adoption of the Law 89-VI, is eliminated (Articles 1.26-1, 10-1 of the Electric Power Industry Law).

*Distribution of Electric Energy Excluded from the Natural Monopoly Sphere*

Services on distribution of electric energy have been excluded from the list of spheres of natural monopolies (Articles 3.8, 4.1.3 of the NML) and, accordingly, are not subject to antimonopoly regulation, including establishment of tariffs.

*Introduction of Liability for Breach of Requirements to the Provision of Technical Conditions for Connection to Electric and Heating Network*

Breach of established procedure and timing for provision of technical conditions for connection to electric and heating network by energy transmission organisation is now subject to a fine in the amount from 25 to 100-fold of monthly calculation index depending on the size of the organisation (Article 301-1 of the Administrative Code<sup>21</sup>). Refusal to accept documents and (or) provide technical conditions for connection to electric and heating network is subject to a fine in the amount from 50 to 200-fold of monthly calculation index depending on the size of the organisation.

*Introduction of Liability for Breach of Requirements to the Provision of Information on Technological Disturbances*

In case of delayed or incorrect provision of information on emerged technological disturbances that caused breach of process of production, transmission or consumption of electric and (or)

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<sup>21</sup> The Code of the Republic of Kazakhstan “On Administrative Violations” dated 5 July 2014 No. 235-V

heating energy, relevant energy producing or energy transmission organisation will be subject to a fine in the amount from 100 to 400-fold of monthly calculation index depending on the size of the organisation (Article 301-2 of the Administrative Code, Article 1.24-2 of the Electric Power Industry Law). If the relevant information was concealed, the organisation will be subject to a fine in the amount from 200 to 1,000-fold of monthly calculation index depending on the size of the organisation.

### **AMENDMENTS IN THE SPHERE OF RENEWABLE ENERGY SOURCES (“RES”)**

According to the President’s Strategy 2050 dated 11 January 2018, Kazakhstan plans to increase the share of alternative energy in Kazakhstan to 30% by 2030. To further develop renewable sources of energy, the Law of Kazakhstan “On Support of the Use of Renewable Energy Sources” No. 165-IV dated 4 July 2009 (the “**RES Law**”) was amended by the Law 89-VI<sup>22</sup> and corresponding bylaws have been adopted.

#### *Currency Indexation of Tariffs*

Important amendment made by the Fixed Tariffs Resolution<sup>23</sup> is indexation of fixed tariffs depending on inflation level and significant change of the exchange rate for the projects with loan obligations in foreign currency. If exchange rate change is equal to or exceeds the previous year figure by 25%, fixed tariffs are subject to change according to the established formula. Such change shall be made as of 1 October each year.

#### *Adjustment of Tariffs by the Government*

The Government of Kazakhstan is now entitled to adjust levels of approved fixed tariffs every year (previously, once in three years) and adjusted fixed tariffs shall enter into force 2 years upon their first official publication (previously, 1 year upon their first official publication).

#### *Introduction of Auction Prices and Auction Mechanism for the Selection of RES Projects*

The RES Law was amended by introduction of so called “auction prices” instead of fixed tariffs and auction mechanism for the selection of RES projects. These important amendments will ensure best prices for the consumers of energy produced by RES and provide transparency in the process of selection RES projects for further implementation.

“From the moment of adoption provisions re auction prices”, i.e. from 14 February 2018<sup>24</sup>, power purchase agreements (the “**PPAs**”) will be concluded between winner of auction and LLP “Settlement Financial Center” (the “**Financial Center**”, the single quasi-state off-taker of the power produced by RES stations) **based on auction price and not fixed tariff**. Fixed tariffs will no longer be used for the new RES projects (with PPA signed after 14 February 2018), however, will be kept for the current RES projects (where PPA was signed before 14 February 2018).

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<sup>22</sup> The Law of the Republic of Kazakhstan “On Introduction of Amendments and Additions to Certain Legal Acts on Electric Energy Issues” dated 11 July 2017 No. 89-VI (the “**Law 89-VI**”)

<sup>23</sup> Resolution of the Government of the Republic of Kazakhstan dated 17 April 2017 no. 207 “On Introduction of Amendments and Additions to the Resolution of the Governments of the Republic of Kazakhstan dated 27 March 2014 no. 271 “On Approval of the Rules of Establishing Fixed Tariffs”

<sup>24</sup> The Order 466 was adopted on 21 December 2017 and entered into legal force from 14 February 2018. Our interpretation of the law suggests that provisions of the law re auction prices shall apply to RES projects from 14 February 2018

The auction prices shall be determined based on results of auction and shall not exceed the maximal auction prices established by the Ministry of Energy.

The maximal auction prices for the first auction that is planned to be conducted in May 2018 are equaled to the current level of the fixed tariffs:

Type of station	Maximal auction price, KZT/kWt per hour (excl VAT)
Wind stations	22.68
Solar stations	34.61
Hydro stations	16.71
Biogas stations	32.23 <sup>25</sup>

Like the fixed tariffs, auction prices are stable (cannot be unilaterally changed by the Government if PPA is already signed)<sup>26</sup>. They are also subject to annual indexation due to inflation and national currency (KZT) fluctuations (the latter applies only for RES projects with loan obligations in foreign currency)<sup>27</sup>. By analogy with the fixed tariffs, the auction prices will also be valid for 15 years from the moment of first energy supply to the electrical lines of energy transmission organisations<sup>28</sup>.

The Order of the Minister of Energy of the Republic of Kazakhstan No. 466 dated 21 December 2017 (the “**Order 466**”) determines the rules of organising and holding auctions, including qualification requirements for auction participants, the content and procedure for submitting applications, types of financial guarantee for participation in auctions and conditions of their deposit and return, the procedure for summing up the results and determining the winners.

Based on the Order 466, the total capacity planned for the selection in 2018 will be 1000 MW, divided by the types of power plants:

- (i) solar power stations – 290 MW;
- (ii) wind power stations - 620 MW;
- (iii) hydroelectric power stations - 75 MW;
- (iv) Bio ES - 15 MW.

The Ministry of Energy of the Republic of Kazakhstan shall, at least 3 three months prior to the proposed date of auction, develop and publish on its Internet resource a schedule for holding auctions for a calendar year. Once published, auction schedule cannot be changed. The schedule contains information on the land plots planned to be allocated for the construction of the RES facility and the points of connection to the electrical networks of the energy transmission

<sup>25</sup> The Order of the Ministry of Energy of the Republic of Kazakhstan dated 30 January 2018 No33 “On Approval of Maximal Auction Prices”

<sup>26</sup> Article 8-1.3 of the RES Law

<sup>27</sup> Article 8-1.2 of the RES Law

<sup>28</sup> Article 104 of the Order of the Minister of Energy of the Republic of Kazakhstan “On Approval of the Rules for Centralised Purchase and Sale by the Settlement Financial Center of Electric Energy Produced by the Objects Using RES, Recalculation and Redistribution of by the Settlement Financial Center of the Relevant Share of Electric Energy per One Qualified Conditional Consumer Based on the Results of the Year” dated 2 March 2015 No 164

organisations, indicating the maximum permissible capacity and the number of possible connections.

The auction is organised and conducted in the electronic system by Joint-Stock Company “Kazakhstan Electricity and Power Market Operator” (“**KOREM**”) and is aimed at selecting projects for the construction of new facilities for the use of renewable energy sources and determining the auction prices of electricity produced by renewable energy sources.

In order to participate in the auction, participants confirm the qualification requirements for legal capacity and solvency by providing the following documents:

1. copy of the charter;
2. copy of a certificate of state registration/re-registration of a legal entity;
3. copies of the decision of the relevant body of the legal entity on the appointment of the director;
4. power of attorney for a representative (in case the representation of interests is not exercised by the director);
5. information on the details of the legal entity (bank details, address, contact numbers, e-mail);
6. a document confirming the financial security for the application for participation in the auction (bank guarantee or standby letter of credit).

Foreign legal entities provide similar documents in accordance with the legislation of the country in which they are registered with a mandatory provision of notarised translation of the documents into Kazakh and Russian languages.

Financial security of the bidder can be provided either as a bank guarantee or a standby letter of credit issued by the bank with high credit rating (of a level and by rating agency as provided by the Order 466) and is KZT 2,000 per kWt of established capacity multiplied on capacity indicated in the application of the bidder.

The financial security shall be returned by the Financial Center within three business days from the date the participant submits a written request to the Financial Center upon one of the following:

1. the participant did not win the auction;
2. the participant won the auction and concluded PPA with the Financial Center.

The winner of auction is automatically included by the Ministry of Energy to the list of energy producing organisations using RES (the “**RES List**”) and plan of placement of RES objects in the territory of the Republic of Kazakhstan (the “**RES Plan**”). This is very important legal amendment for the potential bidders since without inclusion to both the RES List and the RES Plan, no PPA can be concluded. Previously, RES producers had to provide multiple documents to be included to the List and the Plan, and criteria used by the Ministry of Energy for the inclusion to the List and the Plan were not clear. Now they just have to win the auction to be included into both.

*Introduction of Financial Security for the Performance under PPA*

The RES Law was amended by introduction of financial security for the performance of PPA. The winner of auction shall apply to the Financial Center with the request to conclude PPA and provide, *inter alia*, evidence of financial security for the performance of the PPA.

Financial security of the winner can be provided as a guarantee deposit, bank guarantee or a standby letter of credit issued by the bank with high credit rating (of a level and by rating agency as provided by the Order 164<sup>29</sup>) and is KZT 10,000 per kWt of established capacity multiplied on capacity indicated in the register of auction winners<sup>30</sup>.

30% of the financial security will be withdrawn by the Financial Center if the energy producing organisation does not start the construction of the station within 12 months from the moment of PPA conclusion.

The rest of financial security will be withdrawn by the Financial Center if the energy producing organisation does not complete the construction of the station within: (i) 24 months for solar projects; (ii) 36 months for wind and biogas projects; and (iii) 48 months for hydro projects.

It is not clear if the financial security can be withdrawn by the Financial Center in case of breach by the energy producing organisation of any other provisions of PPA.

#### *Introduction of Qualified Conditional Consumer*

The RES Law now contains the concept of so called “qualified conditional consumer”.

Generally, the consumers of the Financial Center are “conditional consumers” that are energy producers using “traditional” sources of energy such as coal etc. Conditional consumers are obliged by law to purchase energy produced by RES producers from the Financial Center at a special “tariff for support of RES” that is calculated based on expenditures of the Financial Center. This arrangement is one of the sources of the Government to support RES producers.

The newly introduced “qualified conditional consumers” will have more favourable conditions, namely, the expenditures of the Financial Center will be distributed among conditional consumers (and, as we understand, included into their “tariff for support of RES”), however, will NOT be distributed among qualified conditional consumers.

Qualified conditional consumer is a group of persons including conditional consumer and RES energy producer that was not included to the RES List and that either consumes all the produced RES energy for its own purposes or sells RES energy to the consumers other than the Financial Center (i.e. does not have PPA).

We understand that this amendment was aimed to encourage conditional consumers to establish RES energy producers.

To the best of our knowledge, there is no qualified conditional consumer in Kazakhstan at the moment.

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<sup>29</sup> Article 94 of the Order 164

<sup>30</sup> Article 96 of the Order 164

## AMENDMENTS IN THE SPHERE OF PUBLIC PRIVATE PARTNERSHIP (“PPP”)

### *Adoption of PPP Template Documentation*

The Resolution on Amendments to the Template PPP Bid Documentation and Template PPP Agreement<sup>31</sup> (the “**PPP Documentation Resolution**”) came into effect on 11 August 2017.

The PPP Documentation Resolution approved template PPP bid documentation and template PPP agreement in the following industries (areas) of economy:

- education (kindergarten);
- housing construction (residential complex);
- housing and utilities infrastructure (street light network);
- health care (outpatient clinic);
- physical training and sports (fitness and health centre);
- health care (polyclinic);
- education (dormitory of education organisation);
- transport (bus terminal);
- environment (waste recycling plant with disposal site);
- agriculture (utility-service centre).

### *Amendments to the List of Objects Not Eligible for PPP Projects*

The Resolution on Approval of the List of Objects Not Eligible for PPP, including Concessions<sup>32</sup>, came into effect on 19 November 2017 and replaced previously adopted decrees of the President of Kazakhstan.

Mainly the list remains unchanged with the following amendments:

- property, organisations and objects of military technical use and organisations of special state bodies required to ensure national security of Kazakhstan are excluded from the list of objects not eligible for PPP projects;
- healthcare organisations carrying out activities in the area of blood banking and HIV/AIDS prevention may purchase medical equipment and its maintenance service within PPP;
- cultural valuables are included to the list of objects not eligible for PPP projects;
- collection and depositaries of agents of special danger infections and industrial microorganisms are included to the list of objects not eligible for PPP projects.

### *Public Private Partnership Contract on the Service Model of Informatisation*

The Law 128-VI<sup>33</sup> amended the Law of the Republic of Kazakhstan No. 418-V dated 24 November 2015 “On Informatisation” (the “**Law on Informatisation**”) and the PPP Law<sup>34</sup> by

<sup>31</sup> Order of the Minister of National Economy of the Republic of Kazakhstan dated 27 March 2017 no. 127 “On Introduction of Amendments and Additions to the Order of Acting Minister of National Economy of the Republic of Kazakhstan dated 25 November 2015 no. 724 ‘On Approval of the Template Bid Documentation of Project of Public-Private Partnership (the “**PPP**”) and Template Agreement of Public-Private Partnership according to Ways of Implementation of Public-Private Partnership in Certain Industries (Areas) of Economies”’.

<sup>32</sup> Resolution of the Government of the Republic of Kazakhstan dated 6 November 2017 no. 710 “On Approval of the List of Objects that cannot be Provided for Implementation of Public-Private Partnership, including Concession”.

introduction of the concept of so called “public private partnership contract on the service model of informatisation” (the “**PPP Service Model Contract**”).

Article 31.2 of the PPP Law now specifically excludes the PPP Service Model Contract from the scope of the PPP Law. Under Article 31.2 of the PPP Law, selection of the private partner and conclusion of the PPP Service Model Contract is regulated by the Law on Informatisation and relevant bylaws without application of the PPP Law.

“Service model of informatisation” is, in brief, automatic centralised process of providing state functions and state services by creation, development and provision of information and communication services (such as, for example, services provided by electronic government website egov.kz) (Article 1.2), 1.3) of the Law on Informatisation).

The PPP Service Model Contract is a service contract that defines the rights, responsibilities, liability of the parties and other conditions for the creation, development and provision of information and communication services. The state partner, the operator of information and communication infrastructure “e-government” and a private partner that is a provider of service software products or information and communication infrastructure facilities, are the parties to the PPP Service Model Contract (Article 1.3-2) of the Law on Informatisation).

The list of projects to be implemented based on PPP Service Model Contract shall be approved by the Ministry of Information and Communication of the Republic of Kazakhstan provided that there is positive conclusion of the Ministry of Finance in relation to financial solvency of such PPP projects (Article 45.5.2) of the Law on Informatisation).

The provider of services under the PPP Service Model Contract is selected by tender process (Article 45-1 of the Law on Informatisation).

The Law on Informatisation establishes the following qualification requirements for the potential providers of services under the PPP Service Model Contract:

1. legal capacity (for legal entities) or civil capacity (for individual entrepreneurs);
2. solvency and no tax debt;
3. financial and (or) material, and (or) labor resources necessary to fulfill obligations under the PPP Service Model Contract;
4. no bankruptcy or liquidation proceedings; the potential provider’s property, the book value of which exceeds ten percent of the value of the relevant fixed assets, shall not be seized; the potential provider’s financial and economic activities shall not be suspended in accordance with the legislation of the Republic of Kazakhstan;
5. no facts of non-fulfillment and (or) improper performance of obligations under PPP contracts concluded during the last three years on the basis of a court decision that entered into legal force, recognising the potential provider as non-reliable potential private partner (Article 45-2 of the Law on Informatisation).

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<sup>33</sup> The Law of the Republic of Kazakhstan No 128-VI dated 28 December 2017 “On Amendments and Additions to Some Legal Acts of the Republic of Kazakhstan on Informatisation and Communication Issues”

<sup>34</sup>The Law of the Republic of Kazakhstan dated 31 October 2015 No. 379-V “On Public Private Partnership”

## **AMENDMENTS TO THE BUDGET LEGISLATION**

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The Law on Amendments to Budget Legislation<sup>35</sup> (the “**Budget Improvement Law**”) came into effect on 17 December 2017, except certain provisions.

The purposes of the Budget Improvement Law are, *inter alia*, to facilitate process of PPP projects implementation.

The Budget Improvement Law amends 2 codes and 5 laws of the Republic of Kazakhstan.

### *Introduction of Business-Plan of PPP Project with Elimination of Concepts of PPP Project*

The Budget Improvement Law excluded requirement to develop concept of PPP project. Private partner in case of direct negotiations with public partner shall develop business-plan instead of the concept of PPP project. If no state support measure is expected, state conclusion on business-plan is not required. Public partner shall develop investment proposal.

Requirement to adopt concession proposal is excluded. Instead, informational list containing description of the PPP project shall be submitted as a part of PPP bid documentation (Article 37.2 of the PPP Law).

### *Exclusion of Two Types of State Expertise for Approval of PPP Project*

Pursuant to the amendments, concession proposal is no longer required, this means one expertise is excluded from the procedure of approval of concession proposals, i.e. timing required for approval is shortened (Articles 151.1, 154-1, 154-2, 155, 155-1, 155-2 of the Budget Code<sup>36</sup>, Articles 1.12, 15-1, 17.1.2-2 of the Concessions Law<sup>37</sup>, Article 10.1 of the PPP Law).

Another expertise excluded from the list of expertise required for approval of PPP project is expertise of draft concession agreement, including in case of amendment of concession agreement (Article 9 of the Concessions Law, Article 26 of the PPP Law).

### *Introduction of Program PPP*

The Budget Improvement Law introduced so-called “Program PPP”. If implementation of a PPP project is provided for by a state or governmental program and such program establishes its basic parameters, then general rules on approval of PPP projects and choice of private partner do not apply. Basic parameters include purposes and tasks, institutional scheme, expected payments from budget funds, measures of state support, beneficiaries under PPP agreement (Article 154-1 of the Budget Code, Articles 7, 31 of PPP Law).

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<sup>35</sup>Law of the Republic of Kazakhstan dated 30 November 2017 no. 112-VI “On Introduction of Amendments and Additions to Some Legislative Acts of the Republic of Kazakhstan on Issues of Improvement of Budget Legislation”.

<sup>36</sup> The Budget Code of the Republic of Kazakhstan dated 4 December 2008 No. 95-IV

<sup>37</sup> The Law of the Republic of Kazakhstan dated 7 July 2006 No. 167-III “On Concessions”

*Elimination of Requirement to Develop Feasibility Study for Certain Types of PPP Projects*

Development of feasibility study is no longer required for the projects with developed design documentation and projects implemented on basis of template documentation, template design decisions and repeated projects (Article 154-3.10 of the Budget Code, Article 20-1.2.2 of the Concessions Law).

*Further Simplification of Requirements Applicable to Certain Types of PPP Projects*

Following adoption of the Budget Improvement Law, not all state obligations under PPP projects are subject to registration with the Ministry of Finance of Kazakhstan, but only those of the Government of Kazakhstan. State obligations of local executive bodies shall be registered with relevant local departments (Article 161 of the Budget Code).

Similarly, now not all PPP projects require adoption of resolution of the Government of Kazakhstan for their registration, but only those of particular significance (Article 161 of the Budget Code).

Acceptance of state obligations of the Government requires approval of the relevant resolution of the Government only in relation to PPP projects of particular significance, other PPP projects require only positive approval of relevant budget committee (Article 162 of the Budget Code).

Acceptance of state obligations of local executive bodies requires decision of local maslikhat (local representative body) of oblast, city of republican significance and capital (as before) or region (city of oblast significance), lower level of state authority (Article 163 of the Budget Code).

Committee for review and selection of concession applications is convened by order of the Prime Minister of Kazakhstan for concession projects of particular significance or organiser of a bid for other projects, rather than by the Government of Kazakhstan or local executive bodies of oblasts (city of republican significance, capital) which also simplifies the procedure of approval of the project (Articles 8, 19.4 of the Concessions Law).

*Possibility to Amend Bid Conditions and Initial Concession Application for Concession Projects of Particular Significance in case of Significant Change of Exchange Rate of National Currency*

If exchange rate of national currency during the bid for the project of particular significance changes significantly (although there is no established criterion on which change shall be considered significant), bid conditions and initial parameters and characteristics of concession application may be amended on the basis of minutes of negotiations and decision of committee subject to approval of the republican budget committee (Article 20.4-1 of the Concessions Law).

*Introduction of Rules for Determination of Cost of PPP Object*

Total amount of co-financing of PPP projects (i.e. state support measures and payments from state budget) and compensation of investment expenses shall not exceed amount of construction and (or) reconstruction of PPP project. Following adoption of the Budget Improvement Law, methods for determination of such total amount shall be approved by the Ministry of National Economy of Kazakhstan (Article 27 of the PPP Law).

*Introduction of Minimum Term of Guaranteed Uptake under PPP agreement*

The Budget Improvement Law introduced a minimum term for guaranteed uptake of goods, works and services within PPP agreement. Such minimum term constitutes three years with right of prolongation under PPP agreement (Article 27 of the PPP Law).

*Abolishment of the Register of Potential Private Partners*

Before the Budget Improvement Law, the National Chamber of Entrepreneurs was responsible for keeping the register of potential private partners. Such register was used for the selection of private partners according to simplified procedure: private partner was determined from this register without further qualification-based selection. The Budget Improvement Law abolished keeping this register and relevant procedure of private partner selection (Article 28, 43.2 of the PPP Law).

*Amendment of Material Provisions of PPP Agreement*

PPP agreements shall mandatory contain certain provisions provided by the law. According to international practice the list now includes mechanism on settlement of currency risks and procedure of compensation of expenses of parties in case of early termination of the agreement (Article 46.1 of the PPP Law).

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*Sincerely yours,*

***Shaimerden Chikanayev***

*Partner*

*Email: [schikanayev@gratanet.com](mailto:schikanayev@gratanet.com)*

*Mob: 7701 7878020*

***Marina Kahiani***

*Partner*

*Email: [mkahiani@gratanet.com](mailto:mkahiani@gratanet.com)*

*Mob: 7701 7251269*

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