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Kazakhstan: Some issues of payments for the right to use intellectual property



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Over the past few years, there has been an increasing number of appeals from Kazakhstani companies related to requests from the tax inspectorate in terms of paying royalties for the use of trademarks and software (intellectual property – IP).

If no license agreement is entered into, it is defined as on a gratuitous use basis, or the royalty rate is “suspiciously low”, the tax inspectorate considers the gratuitous use of the IP to be unjust enrichment and demands to pay 10 percent of the amount of unpaid royalties to the budget and fines for non-payment of such taxes.



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To determine this tax and the amount of fines, the tax authorities often require the user to conduct an assessment of IP, and in almost all cases, since there are no approved methodologies for such assessments or at least recommended royalty rates, such assessments are very challenging. Users of rights to IP usually cannot conduct such assessments themselves, do not know to whom to turn and do not want to incur additional costs. The tax authorities themselves cannot conduct such assessments, in particular due to the lack of appropriate in-house experts and the lack of a budget to pay for the work of private appraisers. Correspondence related to the request of the tax authorities is considerably time-consuming,

and, in most cases, a reasonable answer eliminates the need to pay additional charges to the budget.

Another problem associated with already concluded supply contracts, agreements and licenses for the use of IP is that although the contracts mention the possibility of transferring the right to use IP to Kazakhstani companies in the future, along with the transfer of goods, the provision of technical assistance or services from IP owners, in fact the right to use is not transferred. In these cases, it is necessary to carefully analyze the contracts themselves, the wording used in them, additional agreements, acts of work performed and other documentation to justify the absence of the transfer of the right to use the IP, which could have been avoided if the contracts initially contained clear and precise wording and the subject of the contract would not cause doubts or ambiguous interpretation of its provisions.

Clearly, in order to avoid such problems, it is best to review contracts at the stage of their drafting in order to exclude ambiguous interpretation of the contractual provisions, however, foreign companies often do not want to do this, referring to their “standard international practices”. These practices are obviously convenient for IP owners, but their inconsistency with the legislation of Kazakhstan or the ambiguity of the wording in the contracts causes great inconvenience for Kazakhstani companies.

The requirements to specify royalties in a separate line are also imposed by the customs authorities, since the rates for the royalties are different to the rates for the underlying goods. There are certain inconveniences for importers, but they sometimes lead to savings, since it is possible to divide the cost (to deduct the royalties often taxed at a reduced rate of no more than 10 percent as per the agreements to avoid double taxation). To summarize the above, it is advised to draft contracts in advance with experts in tax law and intellectual property, to conclude and, where necessary, to register license agreements or, if the immediate conclusion of contracts is required, to conduct the above-mentioned review and modify the contract as appropriate before entering it.

According to the Tax Code of the Republic of Kazakhstan (paragraph 15 of Article 243, Deductions for Certain Types of Expenses), “a taxpayer engaged in the production and/or sale of goods under the trade name, trademark and/or service mark owned and/or used by such a taxpayer (including on the basis of a license or sublicense contract (agreement) in the manner prescribed by the legislation of the Republic of Kazakhstan, and/or international treaties ratified by the Republic of Kazakhstan), shall deduct the costs of activities aimed at maintaining and/or increasing the sales of such goods, whether or not owned by him.” In other words, all expenses for the promotion of goods with registered trademarks can be attributed to deductions. Even for those goods that have not yet been imported into Kazakhstan, but the trademark used on them has already been registered. It is advised to register your trademarks and to require your partners who supply their products to Kazakhstan to register their trademarks (or license agreements, which is better) in Kazakhstan. Regarding royalties and deductions, please also like to note the following.

In accordance with subparagraph 1 of paragraph 1 of Article 1 of the Tax Code, royalty payment is for:

- the use or right to use copyrights, software, drawings or models, except for full or partial sale of proprietary (exclusive) rights to intellectual property; the use or right to use patents, trademarks or other similar types of rights;
- the use of “know-how”;
- the use of or the right to use motion pictures, video films, sound recordings or other means of recordings.

According to subparagraph 23) of Article 264 of the Tax Code, expenses for the acquisition from a non-resident related party of management, consulting, consultancy, audit, design, legal, accounting, advocacy, advertising, marketing, franchising, financial (except for remuneration expenses), engineering, agency services, royalties, rights to use intellectual property are not subject to deduction.

In turn, in accordance with subparagraphs 3–2) of paragraph 1 of Article 288 of the Tax Code, the taxpayer has the right to reduce taxable income for the costs of acquiring from a non-resident related party of management, consulting, consultancy, audit, design, legal, accounting, advocacy, advertising, marketing, franchising, financial (except for remuneration expenses), engineering, agency services, royalties, rights to use intellectual property (hereinafter referred to as “intangible services”) in the total amount not exceeding three percent of taxable income. In the light of the above, these provisions of the Tax Code apply to all taxpayers regardless of the activities they carry out, that is, of any type of economic activity.

At the same time, clause 4 of Article 1 of the Tax Code provides that the concepts of civil and other branches of legislation of the Republic of Kazakhstan used in the Tax Code will apply in the meaning in which they are used in these branches of legislation of the Republic of Kazakhstan, unless otherwise provided for by the Tax Code.

Consequently, in accordance with paragraph 1 of Article 125 of the Civil Code of the Republic of Kazakhstan, the exclusive right of an individual or a legal entity to the results of intellectual creative activity and equivalent means of identification of a legal entity, products of an individual or a legal entity, works or services performed by them (company name, trademark, service mark, etc.) is recognized as intellectual property in the cases and in the manner established by this Code and other legislative acts. Therefore, royalties are understood as the above-given concept provided for in subclause 52) of Clause 1 of Article 1 of the Tax Code. In turn, the right to use intellectual property has the meaning as provided for in the relevant branches of the legislation of the Republic of Kazakhstan.

Example: the taxpayer’s taxable income amounted to 10,000,000 tenges, the size of the limitation in accordance with the provisions of the Tax Code will be 300,000 tenges ($10,000,000 * 3\% = 300,000$); the amount of expenses for the purchase of “intangible” services amounted to 200,000 tenges. Accordingly, the taxpayer has the right to reduce the taxable income by the entire amount of the costs for the purchase of “intangible” services, that is, the

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taxable income subject to the corporate income tax will be 9,800,000 tenges (10,000,000 - 200,000).

It's interesting that the possibility of attributing these costs to deductions does not apply to inventions, utility models, industrial designs and designations of origin of goods, but it is as it is.

Source: <https://www.roedl.com/insights/kazakhstan-issues-payments-intellectual-property>