Uzbekistan Market entry 2024: Navigating Tax, Legal and Regulatory Landscapes

15 March 2024

Agenda

1. Brief overview of general corporate tax regime and available tax incentives in Uzbekistan
2. Common legal forms for business, EPC structures and key cross border tax considerations
3. Foreign exchange control regulations
4. New Labor Code and developments in individual taxation
5. Transfer pricing

Welcome speech:

Abdulkhamid Muminov
Country Managing Partner

Jamshid Juraev
Partner, Tax and Legal services

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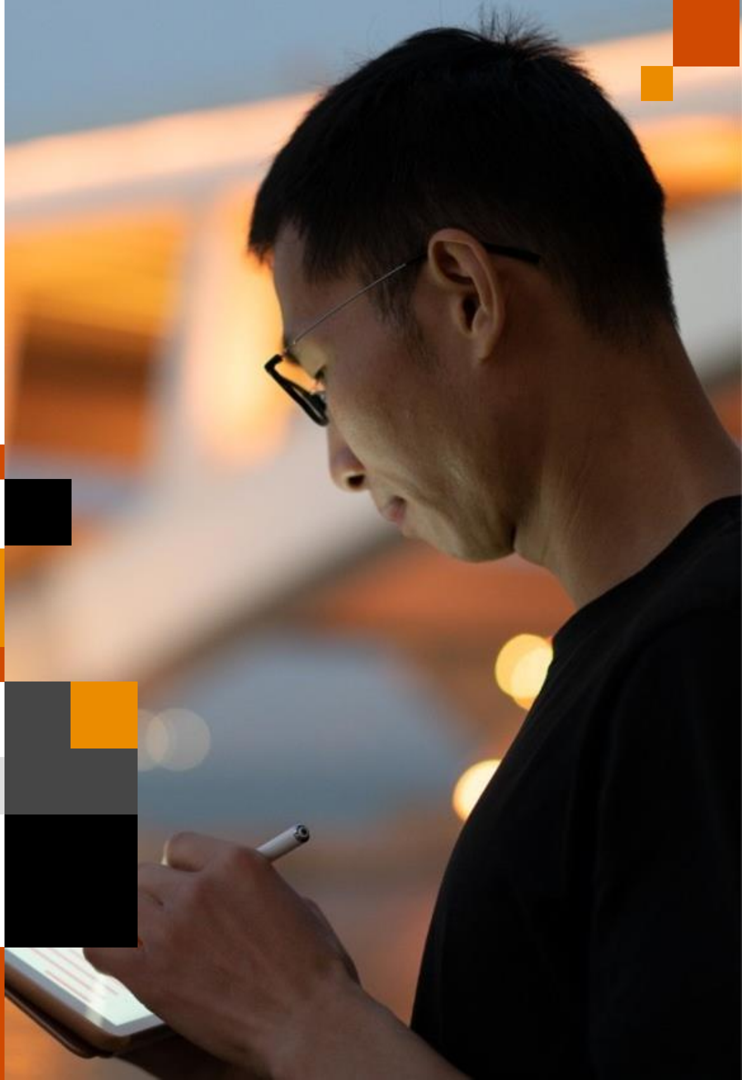
Brief overview of general corporate tax regime and available tax incentives



Speaker:

Yevgeniy Venediktov
Director, Tax services

Overview of applicable tax rates

Tax rate	2024
PIT	12%
Corporate Income Tax	15% (0% - export, except raw materials)
Pension Contribution	0.1%
Employers Social Tax	12%
Dividend WHT (non-residents)	10% (5% from Joint-Stock Companies)
Property tax	1.5%
VAT	12% (0% - export)
Unified tax (for entities with annual revenue less than $80k)	4%

Overview of available tax benefits for certain activities

Special Economic Zones (SEZ)

22 SEZ

Exemption from:
- Land tax
- Property tax
- Water usage tax
- Customs duties for certain imported equipment, commodities, materials

CIT exemption (depending on the investments amount):
- 3 years – $3M-5M
- 5 years – $5M-15M
- 10 years – $15M+

FDI in certain manufacturing industries

Targeting industries, incl.:
- Textile
- Chemicals
- Metals
- Oil refinery
- Construction materials
- Food

Exemption from Land tax, Property tax and Water usage tax (depending on the investments amount):
- 3 years – $300k-3M
- 5 years – $3M-10M
- 7 years – $10M

Sectoral tax incentives & other highlights

10 year exemption from Land tax and Property tax for renewable energy producers

Exemption from customs duties and import VAT for with respect to importation of equipment included in the list of equipment, which have no analogues produced in the territory of Uzbekistan. Currently there are 678 positions in the list and there is a procedure for extension.

For certain sectors:
- Electrical and agricultural engineering:
  - 50%-reduction of CIT and property tax
- Exporters:
  - 0% CIT,
  - accelerated 7-day VAT refund (normally 30)
  - compensation of 50% of the transportation expenses
  - delayed payment of customs duties
- Textile:
  - Exemption from land and property taxes
  - Reduced CIT and PIT rates

IFRS:
- Mandatory for certain categories and large taxpayers (i.e. >$8 mln turnover)
- Optional for others
- Replaces local GAAP

IT Park tax regime

Tax benefits:

- Corporate Income Tax – EXEMPTION
- VAT – EXEMPTION
- Property Tax – EXEMPTION
- Land Tax - EXEMPTION
- Social Tax – EXEMPTION
- Customs Payments - EXEMPTION
- Personal Income Tax – 7.5% (vs 12%)
- Dividend WHT for non-residents – 5% (vs 10%)

Note

All residents should pay 1% of gross income to Directorate of IT Park on a monthly basis, provide information on its activities on a quarterly basis and provide a copy of independent auditor's report annually

Other benefits:

- No Work Permits for foreign specialists
- IT visa for 3 years and simplified residence permit procedure
- Salary and dividends to non-resident employees and shareholders could be paid in foreign currency (within the amount of export revenues)
- Export of goods and services through e-platforms without export contracts
- IT Park assists with turn-key company registration
- Virtual office provided by IT Park (no requirement for physical office)

IT Park residents may perform various activities in IT sector including:

- Development of IT software
- IT consulting and education
- IT products modification and implementation
- Data processing and IT-outsourcing
- Development of equipment for data transmission systems, navigation, communication, etc.
- Web-design, cybersecurity and other

Tax administration lifecycle

Registration with the tax authorities + special registration for VAT

Transactions

VAT-invoices are valid only if provided via government's e-documents flow system

All legal entities are required to report Export and Import transactions in the system controlled by commercial banks and the tax authorities

Tax authorities monitor cross-border bank transactions

Tax reporting

Tax reports may be submitted only electronically

Pre-inspection analysis

All tax reports are subject to automatic pre-inspection analysis. If any issues arise, tax review or tax audit may be initiated

Tax review / tax audit

Tax review and tax audit may cover up to 3 calendar years (recently the period was decreased from 5 years to 3 years)

Tax administration criteria

Risk assessment system

Low risk (1 – 29 points)
No tax audits

Average risk (30 – 80 points)
Desktop tax review may be conducted

High risk (81 – 100 points)
Fully-fledged tax audit
Rejection in offsetting VAT

Criteria for risk assessment:

- Tax burden
- Results of tax audit
- Multiple resubmissions of tax reports
- Losses reported for 2+ years
- Other confidential criteria

Sources for risk assessment:

- Tax & financial reports
- Media
- Info from tax audits
- Data from other state authorities or legal sources

Highlights

- Reassessment of risk level every 6 month
- Automated assessment: cross-checking of reported income and expenses in tax reports (e.g. CIT vs VAT)

Sustainability rating

Under Cabinet Resolution #55 dated 30 January 2024, certain incentives will available to business entities as of 1 April 2024 depending on their sustainability rating.

The following incentives are applicable to "AAA"-rated entities:

- Exemption from tax inspections (except for tax audits within the scope of criminal cases);
- Expedited VAT refund process (within 1 day) without statutory inspection procedures.

The following incentives are available to entities rated "A" or higher:

- Expedited refund of overpaid taxes (within 3 days), except for VAT;
- Consolidated accounting of VAT on import of goods and VAT on supply of goods and services.

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Common legal forms for business and EPC structures Key cross border tax considerations

Speakers:

Miras Sandykbayev
Senior Manager,
Tax services

Madina Aliyeva
Senior Manager,
Tax services

Special features on performing activities of foreign entities

Foreign entities considering a project in Uzbekistan may proceed with its activities via either a permanent establishment (PE) or an Uzbek legal entity (ULE). In the table below we briefly summarize key points to consider prior the decision on registration of either of them:

Key features	PE of foreign legal entity	ULE
Legal status	Operationally - similar to the concept of branch Not a separate legal entity - only represents tax status of FLE in Uzbekistan	Separate legal entity
Tax regime	General (CIT, VAT, WHT, payroll, etc.) + 10% tax on PE's net profits on a quarterly basis (the rate could be reduced if DTT provides lower rate for dividends)	General (CIT, VAT, WHT, payroll, etc.), some tax incentives may be allowed
Terms of activities	Shorter-term operations, e.g. one-off project or a number of occasional projects in single location	Long-term business presence
Mandatory financial audit	N/A, but subject to tax compliance	Applicable
Currency control	Operations with locals in foreign currency allowed via FLE's bank account	Operations with locals in UZS only (some hedging instruments could be used to manage the currency risks)

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Key features	PE of foreign legal entity	ULE
Profit repatriation	Without limitations	Without limitations upon payment of withholding tax (standard rate is 10%, could be reduced by DTT)
Allocation of general and administrative expenses of FLE	Could be deductible	Not allowed but some service agreement may be used
Other expenses	Deductible if related to profit generating activity	
Withholding tax	Interest, insurance premiums – 10% Royalty, other income – 20%	Interest, insurance premiums – 10% Royalty, other income – 20%
Transfer pricing regulations	Applicable	

Commonly used EPC structures

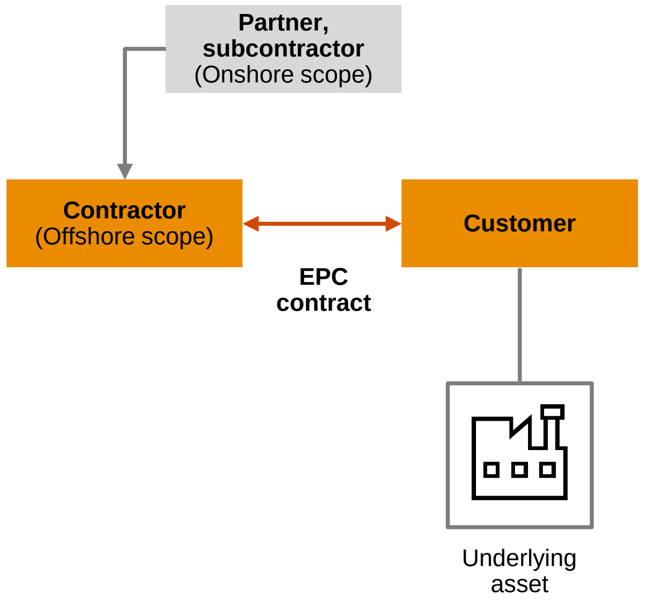
Engaged parties

Customer
Owner of the underlying asset

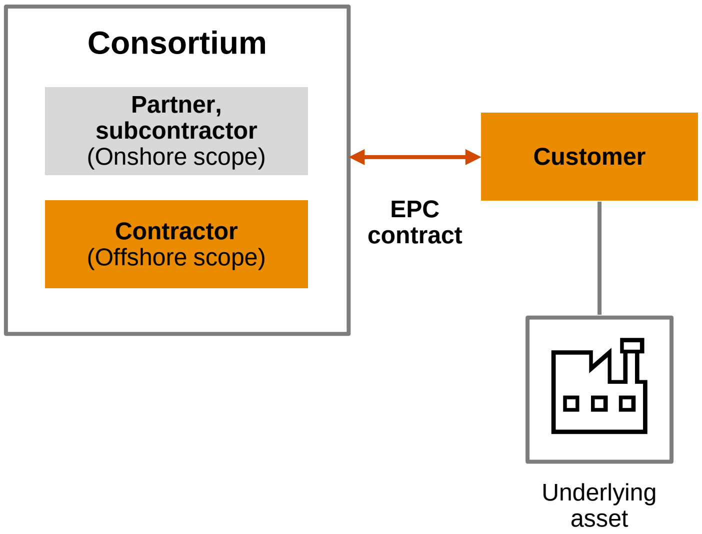
Contractor
Responsible for execution of the Project - may be performing offshore scope (procurement, engineering)

Partner
Responsible for construction / installation works onshore

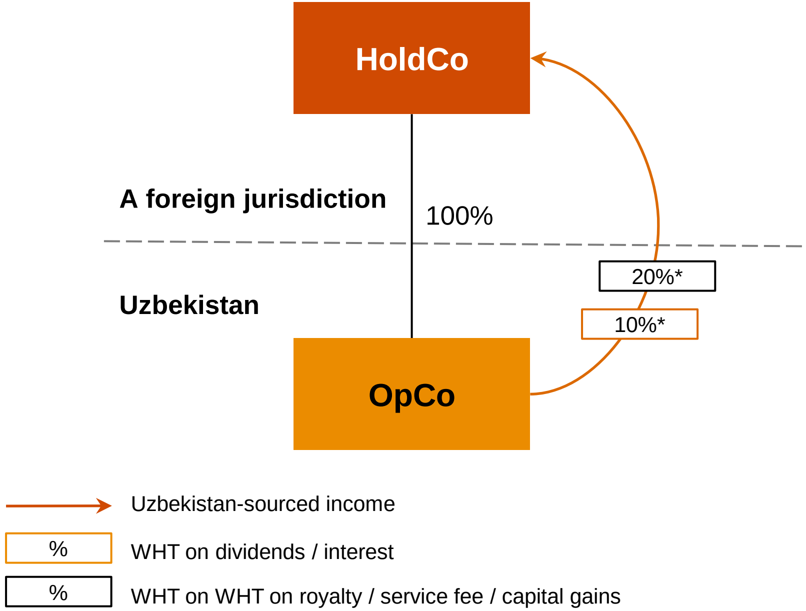
Simple structure – division of contracts



Consortium structure



Key considerations of crossborder taxation



*Rates may be reduced under the relevant DTT

Uzbekistan-sourced income and WHT rates

Statutory rates

- Dividends and interest - 10%;
- Capital gains, royalties and business income - 20%.

Uzbekistan has signed 55 DTTs, 54 of which are effective at the moment. Below is an overview WHT rates under DTTs of Uzbekistan with France, the Netherlands and Switzerland.

	Dividends	Interest	Capital gains	Royalties	Business Income
UZ-CH DTT*	5%	0% / 5%	0% / 20%	5%	0%
UZ-FR DTT*	5%	0% / 5%	0% / 20%	0%	0%
UZ-NL DTT	0% / 5%	0%	0%	0%	0%

Most favored nation regime is available

Key considerations of crossborder taxation

Statutory requirements for application of DTT benefits

- **Tax residency certificate** - in a format meeting requirements of the Tax Code
- **Beneficial ownership** - a set of documents to confirm beneficiary entitlement of a nonresident recipient

Tax incentives available for international financial institutions (“IFI”) / foreign governmental financial organisations (“FGFO”)

- A number of IFIs and FGFOs are eligible for immunity from all types of taxes on the income, assets and operations. These IFI’s include, among others, the following:
  - ✓ European Bank for Reconstruction and Development;
  - ✓ International Financial Corporation;
  - ✓ International Monetary Fund;
  - ✓ Asian Development Bank;
  - ✓ Asian Infrastructure Investment Bank;
  - ✓ Islamic Development Bank;
  - ✓ Islamic Corporation for Private Sector Development;
  - ✓ OPEC Fund.

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Foreign exchange control regulations - key aspects

Speaker:

Vladimir Sokolov
Director, Legal services

Bakhora Akhmedova
Manager, Legal services

Foreign exchange control regulations

National currency

All tariffs, prices for goods, works, and services, as well as charter capital requirements for legal entities in the territory of the Republic of Uzbekistan, and state duties and fees* are determined exclusively in sums

It is **prohibited** to link prices for goods, works, and services in the territory of the Republic of Uzbekistan to foreign currencies and conventional units **

* except for the consular fees
** except for the projects involving foreign investments attracted under PPP agreements and investment treaties with the government of the Republic of Uzbekistan, based on decisions of the President of the Republic of Uzbekistan

Accounts in foreign banks

Local legal entities can open accounts in foreign banks (usually for major investment projects) only based on (1) decisions of the President or the the Cabinet of Ministers of the Republic of Uzbekistan or (2) international treaties.

After opening accounts in foreign banks, ULE shall notify the tax authorities and the Central Bank about:

- opening an account (including its subsequent closing),
- changes in account details the balances, and
- turnovers on these accounts on the quarterly basis

Purchase and sale of foreign currency by residents and non-residents on current international operations, as well as for the purposes of repatriation of direct investments and income of non-residents are carried out without restrictions

Foreign exchange control regulations

Currency control

The purchase and sale of foreign currency on the territory of the Republic of Uzbekistan is carried out exclusively through local banks

The following transactions will be carried out only with the respective decision by the President, the Cabinet of Ministers of the Republic of Uzbekistan or an international treaty:

- transfer of funds in the amount of more than USD 10,000 in terms of investment activities;
- granting credits and loans in the form of cash, goods, and leasing facilities to non-residents by residents;
- transfer of funds of residents from local bank accounts to accounts (deposits) in foreign countries;
- transfer of funds of residents from local bank accounts to overseas for the purchase of real estate

The following transactions are monitored by banks and state authorities:

- transfer of dividends or repatriation of profits to foreign shareholders;
- payment to non-residents for the sale of stocks and shares in the charter capital of ULE and immovable property located in the territory of the Republic of Uzbekistan;
- transfer of funds for the import of goods (works or services) to non-residents registered or holding bank accounts in offshore zones;
- payment of fines to non-residents by residents for not fulfilling obligations under export-import contracts;
- payments made under import contracts, royalty payments;
- payment to a non-resident by a resident under a loan agreement

Foreign exchange control regulations

Accounts of permanent establishments

The following funds may be credited to the foreign currency accounts of permanent establishments of non-residents:

- funds transferred from foreign accounts of non-residents;
- dividends, incomes, and other funds received as a result of investment activity in the Republic of Uzbekistan;
- funds acquired in the domestic foreign exchange market;
- transfers on current international operations

Funds in foreign currency accounts of permanent establishments of non-residents may be used:

- for transfer to foreign accounts of a non-resident;
- for payment of bank commission on operations in foreign currency, expenses related to sending employees on business trips outside the Republic of Uzbekistan (including in cash);
- for sale in the domestic foreign exchange market;
- for current international operations

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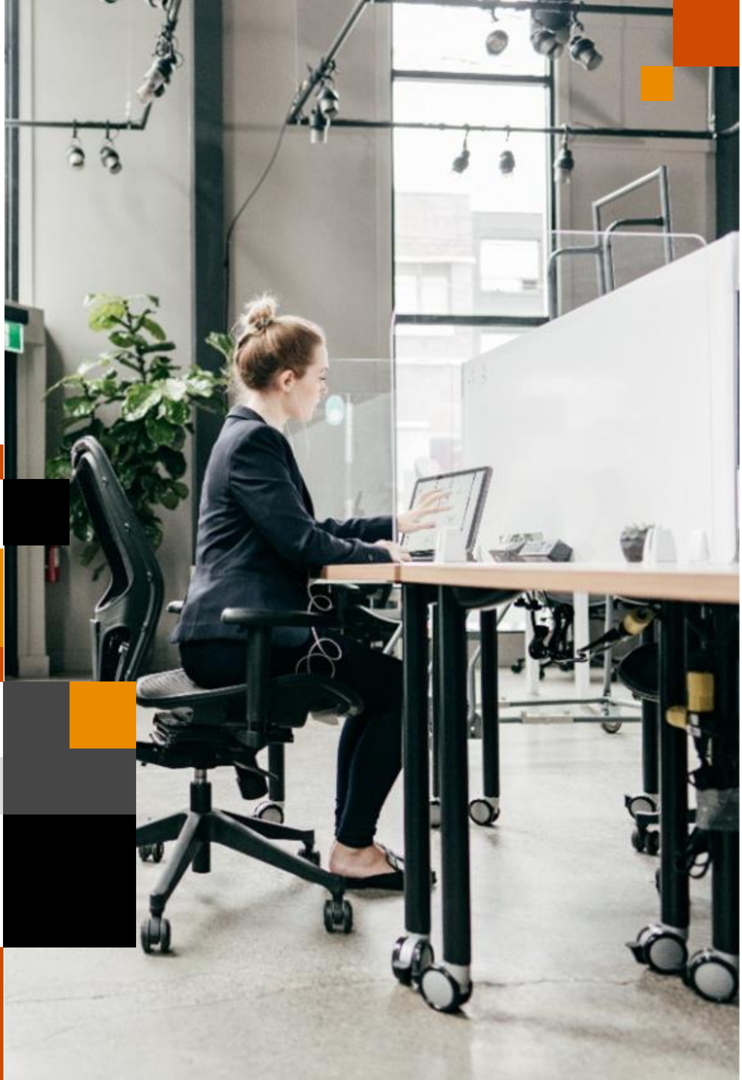
New Labor Code and developments in individual taxation



Speaker:

Alisher Zufarov
Director, Tax services

Aleksandra Morozova
Manager, Tax services

Provisions of the Labor Code effective from April 30, 2023

Salary payment currency	Salaries are paid in **national currency** (sums). Exceptions to this rule may be established by law.	Payment in kind is **prohibited**, except in cases established by the Cabinet of Ministers of the Republic of Uzbekistan.
Engaging foreign citizens in employment	Foreign citizens have the right to carry out labor activities on the basis of **a work permit** or **accreditation**	It is **prohibited** to enter into an employment contract with a foreign citizen without a valid work permit or accreditation.
Calculation procedure and minimum duration of vacation	The duration of vacations is calculated in calendar days. The minimum duration of labor leave is **21 days**. While on leave, the employee retains his place of work and average earnings.	Termination of an employment contract with an employee at the initiative of the employer while on vacation is **not allowed.**

Mandatory local regulations of the Employer

Mandatory local regulations

- Internal labor regulations
- Statement on the protection of personal data
- Occupational safety documents
- Vacation schedule

The concept of a tax resident

A tax resident is an individual who stays in Uzbekistan for 183 days or more during any consecutive 12-month period beginning or ending in the tax period for which the corresponding status is determined. A foreign citizen can also be considered a resident if he stays in Uzbekistan for less than 183 days, but more than in any other country.

Deadlines for filing returns and paying taxes

Residents of the Republic of Uzbekistan staying on the territory of Uzbekistan

The deadline to file 2023 returns is **April 1, 2024.**

The deadline to pay your 2023 income tax liability is **June 1, 2024.**

Residents of the Republic of Uzbekistan who cease their activities in Uzbekistan and travel beyond its borders

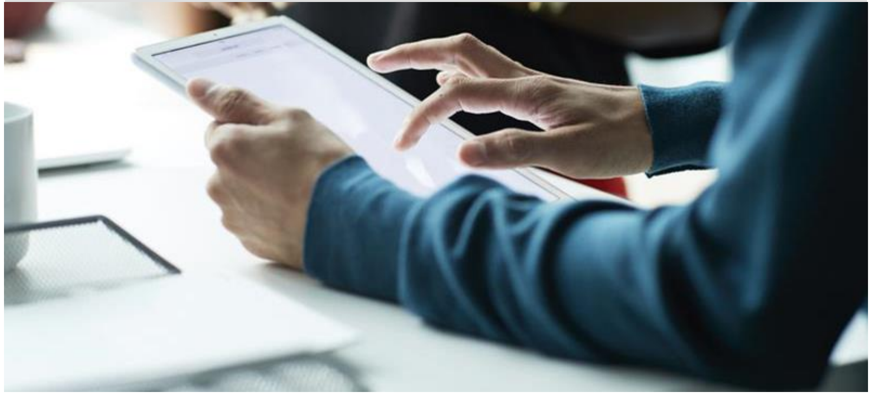
The deadline for filing a “departure” declaration is **1 month before departure.**

The deadline for paying income tax obligations is **15 days before departure.**

Responsibility

Financial liability of an individual

A fine of 20% of the amount of unpaid tax;	An administrative fine of 3 basic units (about 80 US dollars).



Personal income tax (PIT)

Taxable income of a taxpayer allocated to pay for the education of his children (regardless of the age of the children) in professional and higher educational organizations of the Republic of Uzbekistan is not subject to personal income tax from August 1, 2023!

Previously, the personal income tax benefit was applied to children under 26 years of age.

According to Article 391 of the Tax Code, the tax agent has the right to apply the benefit and carry out recalculation within 2023 and return to the employee the amount of personal income tax withheld in excess.

Regarding the use of income to pay for the education of a spouse, the age limit of 26 years remains.

The changes were made in accordance with clause 11 No. Presidential Decree (PD)-67 dated 05/08/2023.

From December 1, 2023, Uzbekistan increased the minimum wage, BCV and minimum pensions, social. benefits

- Minimum wage (minimum wage) – **1 million 50 thousand** soums. per month (increased from **980 thousand** soums);
- Basic calculated value (BCV) – **340 thousand** soums per month (increased from **330 thousand** soums);
- The basic amount for calculating pensions will be **372 thousand** soums. per month (increased from **347 thousand** soums);
- The minimum age pension will be **725 thousand** soums per month (increased from **677 thousand** soums);
- Salaries of employees of budgetary organizations are indexed by 7%.

The changes were made in accordance with Presidential Decree No. UP-196 dated November 17, 2023.

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Transfer pricing: key issues, compliance

Speakers:

Nikolai Milogolov
Manager, Transfer pricing

TP rules - general provisions

General provisions

- Transfer pricing (TP) rules have entered into force in Uzbekistan on 1 January 2022.
- Uzbek TP rules are generally based on the OECD guidance. According to these rules, prices applied in transactions between related parties should be applied as if they were conducted between independent parties (“arm’s-length” principle).
- TP scope covers both transactions between Uzbek tax residents and cross-border transactions.
- If tax authorities have grounds to believe that transfer pricing in a transaction between related parties led to understatement of taxable base, they may apply corresponding adjustments and impose a fine comprising 40% of understated liability.

TP rules - compliance

Key TP compliance considerations

- **Notifications on the controlled transactions** (group of transactions) made through a calendar year must be submitted to tax authorities within statutory deadlines for filing financial statements.

- Within the scope of TP regulation, the tax authorities may request **TP documentation** from taxpayers engaging in transactions that fall under TP scrutiny.

- These documents should cover, among others, information about counterparties, functions of parties to transactions, information about TP method applied etc.

- Tax authorities may request TP documentation starting from 1 June of the calendar year following the year in which these transactions took place. TP documentation should be provided in 30 days from the date of request.

In-scope transactions

<table>
<tr><th colspan="4">1. Between related parties – Uzbekistan residents</th></tr>
<tr><td>Domestic related party transactions</td><td>One party is applying special tax regime or is a SEZ Participant</td><td>One party is applying tax Incentive</td><td>Transaction with extracted mineral if subsoil use tax is calculated based on ad valorem rate</td></tr>
<tr><td>Total revenue from transactions exceeds UZS 5 bln. (about USD 450,000) during the calendar year</td><td colspan="3">Total revenue from transactions exceeds UZS 500 Mln (about USD 45,000) during the calendar year</td></tr>
<tr><th colspan="4">2. Cross-border</th></tr>
<tr><td rowspan="2">Any transaction between related parties</td><td colspan="3">Transactions with either related or non-related parties</td></tr>
<tr><td colspan="2">Commodity cross-border trade:
• Non-ferrous and precious metals
• Fertilizers
• Hydrocarbon and oil products
• Cotton</td><td>“Offshore” transactions with parties resident in the black-listed jurisdictions (including “offshore” PEs of Uzbek companies)</td></tr>
<tr><td colspan="4">Recognized as controlled transactions for TP purposes without any materiality thresholds</td></tr>
<tr><th colspan="4">3. With PEs of foreign companies</th></tr>
<tr><td colspan="4">Any transactions between PE of the foreign company and its related parties (both with residents and non-residents of the Republic of Uzbekistan)</td></tr>
<tr><td colspan="4">Recognized as controlled transactions for TP purposes without any materiality thresholds</td></tr>
</table>

Thank you!