



International
Co-operative
Alliance
Asia and Pacific

LEGAL FRAMEWORK ANALYSIS

CENTRAL ASIA

SUB-REGIONAL REPORT

ICA-EU PARTNERSHIP



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LEGAL FRAMEWORK ANALYSIS

within the ICA-EU Partnership

Sub-Regional Report: CENTRAL ASIA

I. INTRODUCTION

The legal expert Mr. Bakir Urkinbayev conducted the present report of the cooperative legislation of the Republic of Kazakhstan and the Kyrgyz Republic in accordance with the project Legal Framework Analysis within ICA-EU partnership.

The leaders of the Union of Consumer Cooperation of the Republic of Kazakhstan took part in the preparation of this report and the information of the Union of Cooperatives of Kyrgyzstan was used. The report examines only the current cooperative laws that have a direct impact on the cooperative movement of the above countries.

Unlike other forms of business model, a cooperative is responsible for its obligations by all the property belonging to it and is not responsible for the obligations of its members. Cooperative members are not liable for its obligations and bear the risk of losses associated with the cooperative's activities, within the limits of the share value contributed.

Currently, the following laws remain **applicable** in the Republic of Kazakhstan:

- Law of the Republic of Kazakhstan dated October 5, 1995 “On Production Cooperative”. (updates: 07.15.96; 06.19.97; 07.12.01; 03.03.04; 05.05.06; 07.07.08; 10.29.15; 02.27.17;)
- Law of the Republic of Kazakhstan dated May 8, 2001 “On Consumer Cooperative”. (updates: 07/05/06; 05/15/07; 12/24/12; 03/07/14; 05/16/14;)
- Law of the Republic of Kazakhstan dated October 29, 2015 “On Agricultural Cooperatives”. (no updates so far)

In Kyrgyzstan, the main cooperative law is the unified Law “On Cooperatives” dated June 11, 2004 (last update was in July 26, 2018). There is also the Law “On Credit Unions” dated October 28, 1999 (last update 16.12.16) in the country. This law regulates the activities of financial cooperatives - credit unions.

In general, these laws define the legal and economic principles for the formation and operation of cooperatives and their unions in these countries. According to these laws, cooperatives can be established as commercial cooperatives, if the main purpose of their activity is profit recovery or as non-profit cooperatives that operate in the interests of their members, for whom profit recovery is not the main purpose of the activity.

The cooperative movement in Kazakhstan and Kyrgyzstan along with the above laws are guided in their activities by the provisions of their constitutions, civil codes and other regulations of their countries.

An analysis of current laws in **Kazakhstan** shows a large difference in the regulation of cooperatives.

Thus, the imperfection of the law “On the Production Cooperative” resulted in their insignificant share in the total area of agricultural land, in the livestock of cattle, in the production of wheat and milk. The current situation explains the lack of working capital for the development of production, their considerable arrears and, accordingly, their number reduction two times over the past decade. The cooperative principles are violated in production cooperatives, in particular, full economic independence, **the right to receive ownership** for the corresponding share of collective property, **including land**. These factors do not encourage any agricultural producers to work in a production cooperative, which has led to the bankruptcy of most existing cooperatives of this type.

During the study of the current situation, the main factors hindering the development of agricultural cooperation in the Republic of Kazakhstan were revealed: a high level of agricultural producers' distrust, especially of small businesses, to the new structures being created, the fear of losing the only means of production –the land and a low level of legal culture in the villages, the lack of farmers' awareness about the benefits of agricultural cooperatives.

Despite the existence of laws, the regulatory legal acts in force in Kazakhstan do not take into account the specific features of the cooperatives functioning; do not create sufficient legal conditions to unify the agricultural producers, especially small business forms, for the purpose of joint land cultivation, production, marketing, processing, storage, supply them with material and technical resources and other types of service.

At the same time, we note that the Law “On Consumer Cooperatives” is the most “cooperatively friendly” and unambiguously meets the principles of the International Cooperative Alliance: voluntary and open membership, democratic control, economic participation, autonomy and independence, education, training and awareness, cooperation between cooperatives and care for its members.

However, this law does not provide adequate state support and finally has disappeared from the government's view due to the adoption of the new Law “On Agricultural Cooperatives”, which is going to be the main law for cooperatives.

In Kyrgyzstan, the unified Law “On Cooperatives” provides complete freedom in the creation of various types of cooperatives, meets the principles and values of the ICA and, thus, is “cooperatively friendly”. In this context, we emphasize that the cooperative movement in this country is under support of the state, although this assistance is not quite effective yet.

II. NATIONAL COOPERATIVE LAW: KAZAKHSTAN & KYRGYSTAN

I. General Context

There is no single general law on cooperation in **the Republic of Kazakhstan**. Since the Constitution of the country does not define co-operatives, therefore co-operatives of the Republic of Kazakhstan, being associations, are guided by the provisions of the Civil Code in their activities, where the cooperative definition is directly given, as well as by the laws in force “On production cooperative”, “On consumer cooperative” and “On agricultural cooperatives”.

In Kyrgyzstan, unlike Kazakhstan, there is a single Law “On Cooperatives,” which clearly designates cooperatives and fully regulates their activities. The term “cooperatives” is also explicitly defined in the Civil Code of Kyrgyzstan, but is absent in the country's Constitution.

The mentioned laws of both countries emphasize such principles as voluntary entrance and disaffiliation, democratic governance, mutual assistance and protection of the members' interests, availability of information on the activities of the consumer cooperative for all its members, which distinguishes it from other types of business.

In Kazakhstan, unlike the Law “On Consumer Cooperatives”, the current Law “On Production Cooperatives” and the recently adopted Law of the Republic of Kazakhstan “On Agricultural Cooperatives” provide for the creation of cooperatives only in the form of a commercial organization pursuing income recovery as the main goal of the activity.

It is known, the international practice of the cooperative movement provides for the creation of agricultural cooperatives both in the form of a production cooperative and in the form of a consumer cooperative. At the same time, all forms of agricultural cooperatives, especially in economically developed countries, usually do not provide for profit and income recovery as their primary goal.

II. Specific Elements of Cooperative Law

a) Definition and objectives of cooperatives

The current cooperative laws determine the legal status of cooperatives, the organizational, economic and social conditions for their creation, activity, reorganization and liquidation, the rights and obligations of members, the powers and responsibilities of the governing and control bodies.

As noted above, **in Kazakhstan** only the consumer cooperative is a non-profit organization and can engage in business activities only insofar as it corresponds to its by-law goals.

In **both** countries, in general, the laws of the cooperative of their members are regulated in special articles, which state that cooperatives are created at the expense of property (share) contributions to perform certain functions related to meet the interests of their members. The above laws, labor laws and charters govern labor relations in cooperatives. The remuneration amount for the personal labor participation of members in its activities shall be established by the decision of the general meeting.

The main consumers of the results of activities (manufactured or purchased goods, works, and services) are members of the cooperative.

Laws do not prescribe provisions that allow a cooperative to act in the interests of non-members and society as a whole. Such issues, by default, relate to the powers of the general meeting of the cooperative, which is the highest body thereof and authorized to settle any and every issue relating to its activities. There are no certain types of cooperatives in the countries that established by law for social protection of the population.

b) Establishment, cooperative membership and governance

In Kazakhstan, the creation of a cooperative begins with a constituent assembly holding and ends with compulsory state registration as a legal entity. Laws determine that at least two (2) members are required to create a cooperative (at least 3 in the Law “On Agricultural Cooperatives”), but it does not stipulate a situation if the number of members becomes less.

In Kyrgyzstan, cooperatives must also be registered with the justice authorities. A cooperative is considered as created as a legal entity from the moment of its state registration. The number of a cooperative's members must be at least 7, unless otherwise specified in the legislation, based on the specialized activities of cooperatives. There are no provisions in the legislation regarding the case if the number of members is less than 7 members.

Regarding the issue of new member's admission, the laws of **Kazakhstan and Kyrgyzstan** have almost the same provisions defining the possibility of joining a cooperative. According to the laws, a member of a cooperative is free to leave it and there are no restrictions on this.

Each member of the cooperative has one vote regardless of its share size in the property, that is, the principle “one member - one vote” is observed. At the same time, in Kazakhstan, the laws do not stipulate any limitations or exceptions, including that they may be provided for in the charters of cooperatives.

At the same time, in Kyrgyzstan, the law stipulates that each member of a cooperative has the right to attend the meeting in person or via a representative who has a power of attorney. Moreover, if there are less than 20 members in the cooperative, one representative can represent only the interests of one member, if there is more than 20 members in the cooperative, one representative cannot represent the interests of more than 3 members of the cooperative.

In accordance with the law of **Kazakhstan**, the main bodies of the cooperative are the general meeting, the executive body (board), the supervisory board (if necessary) and the audit committee (auditor). The leaders of the cooperative can only be members of the cooperative.

In Kyrgyzstan, the management of the cooperative is carried out by the general meeting, the council of the cooperative (created in the cooperative if the number of members of the cooperative is not less than 50) and the executive body (board). If the number of members is less than 50, the power of the council is transferred to the general meeting of the cooperative members. Not only the cooperative member can be the Chairman and members of the board.

In both countries, the cooperative members can appeal decisions and actions of the executive, control and other bodies of the consumer cooperative at a general meeting or in court.

c) Cooperative financial structure and taxation

The laws of **Kazakhstan and Kyrgyzstan** do not define the minimum contribution for a cooperative creation. Property (share) contribution may be made in cash, securities, things, property rights, including the right to land use and the right to the results of intellectual activity and other property.

The shares of all cooperative members in the cooperative property (in the value of the property) are determined in proportion to their contributions to the cooperative property. The charter of cooperative or the general meeting may establish a procedure for determining and changing the shares, depending on the contribution of each of them to the formation and increment of property. In accordance with the law, in the case of cooperative liquidation, a member of the cooperative has the right to receive the value of a property part remaining after settlements with creditors, or, by agreement of the majority of the cooperative members, a part of this property in kind proportional to its property (share) contribution.

In Kazakhstan, in contrast to the two other laws, the Law “On Consumer Cooperative” provides that income received by the consumer cooperative cannot be distributed among its members and is directed to statutory goals.

The laws in force in **both countries** provide for the right of the cooperative to create various funds, including a reserve fund and a fund for the promotion and social support of its members.

The laws refer such matters as use of various financial instruments and “members-investors” by the cooperative to the competence of the general meeting, the executive body or the cooperative’s charter.

In the case of Kyrgyzstan, the Law does not provide for the possibility to issue financial instruments by the cooperative, as well as admission of “members-investors” to membership.

Previously, legislation included the concept of “an associate member of a cooperative,” which was a cooperative investor per se, but did not participate in the cooperative management. Such a rule was excluded.

According to the laws of **Kazakhstan**, a cooperative cannot be transformed into other types and forms of legal entities. In the case of the cooperative liquidation, a cooperative member has the right to allocate a share in the cooperative property proportional to its property (share) contribution.

In Kyrgyz legislation, there are no specific rules on the capital and assets allocation in the event of liquidation by a decision of the general meeting or the transformation of a cooperative into another organizational and legal form. The conditions and procedure for reorganization, transformation can be provided for in cooperative’s charter.

Regarding the taxation, it is necessary to emphasize that **in Kazakhstan**, production and consumer cooperatives do not have any tax preferences, according to the existing laws.

In the case of agricultural cooperatives, they fall under the provisions of the Tax Code of the Republic of Kazakhstan, where the amount of income tax, social tax, property tax and road tax is reduced for agricultural producers by 70% from the generally established rate for other categories of taxpayers. Tax Code of the Republic of Kazakhstan provides for the tax payment in the amount of 30% of the calculated amount, save for land tax. The road tax is not paid on objects of taxation directly involved in the process of production, storage and processing of its own agricultural products.

However, a special tax regime, in which a 70% discount on tax payments is established, is provided only for rural production cooperatives with land plots on their balance sheets. Due to the fact that majority of cooperatives do not own land plots so they can not enjoy the benefit of this tax regime. *(At the same time, according to the available information, this restriction can be removed, since such amendments to the existing law are pending in the Parliament).*

In contrast to other economic entities, agricultural cooperatives in accordance with the Tax Code of the Kyrgyz Republic are provided with a number of preferences.

Cooperatives are exempt from income tax, sales tax, value added tax, real estate tax at rate of 50 percent (recent changes in the Tax Code of Kyrgyz Republic dated August 4, 2018).

The supply of its own agricultural products by the agricultural cooperative, as well as its processed products, is a VAT free supply.

The supply of agricultural products and processed products by an agricultural cooperative received from agricultural producers who are members of the cooperative is a VAT free supply.

The supply of goods, works, services by an agricultural cooperative to members of this cooperative is a VAT free supply.

Dividends received by a resident of the Kyrgyz Republic from participation in domestic organizations are income not subject to income tax.

An agricultural cooperative, as tax agents, withholds and pays a fixed amount of income tax on each employee, calculated based on the minimum estimated income, from the wages of employees.

According to the Tax Code of the Kyrgyz Republic, a dividend is a part of the taxpayer's profit, including cooperative payments to members of agricultural cooperatives. However, the Law "On Cooperatives" distinguishes the concept of "dividend" from the concept of "cooperative payments", which should be noted about the inconsistency of the two regulatory legal acts to each other.

d) Other specific features

The laws of **Kazakhstan and Kyrgyzstan** determine that state bodies and local governments do not have the right to interfere in the activities of the cooperative, with the exception of cases stipulated by

legislative acts of the countries. Acts of state bodies or acts of local governments that violate the rights of the cooperative may be declared as invalid in the manner prescribed by the legislation. Damage, including lost profits, caused to cooperative as a result of an unlawful act or inactivity of state bodies and local government or their officials, shall be compensated in accordance with the procedure established by the legislation.

The **Kazakhstan** Law “On Agricultural Cooperatives” determines the role of government bodies much broader and it further notes that the authorized state body in order to stimulate the creation of agricultural cooperatives:

- 1) provides information, consulting and methodological assistance in the development and implementation of measures for the dissemination and introduction of experience in creating and operating agricultural cooperatives, including through Internet resources;
- 2) develops proposals:
 - to create a favorable tax, financial and credit, investment policy regarding the activities of agricultural cooperatives;
 - for state support of agricultural cooperatives in accordance with the legislation of the Republic of Kazakhstan;
- 3) promotes the training, retraining and advanced training of personnel for agricultural cooperation and implementation of research on agricultural cooperation;

According to the law, local representative and executive bodies should provide similar support to agricultural cooperatives.

The Law “On Production Cooperative” does not separately indicate the role of the state in the activities of the cooperative.

The existing laws in **Kazakhstan and Kyrgyzstan** clearly provide for the self-control of the cooperative through the creation of a supervisory board, an audit commission, and the involvement of an independent auditing company. It is also indicated that any member of the cooperative may request an audit of the financial activities of the cooperative, and in case of refusal to apply to the relevant judicial instances.

In **Kazakhstan**, cooperatives can unite into unions and associations, but they additionally use the Law “On Non-Profit Organizations” for this, because the existing cooperative laws do not clearly indicate such a possibility.

In **Kyrgyzstan**, legislation provides for the possibility of uniting cooperatives into cooperative unions, and such an organization is a non-profit organization.

Cooperation between the cooperatives is not specified in the laws of the both countries and, accordingly, do not provide for special forms and rules. It is believed that the legislators attributed this to the discretion of the cooperatives and their bodies.

III. DEGREE OF “COOPERATIVE FRIENDLINESS” OF THE NATIONAL LEGISLATION

In **Kazakhstan and Kyrgyzstan**, despite the existence of laws, the existing legal acts do not take into account the specific features of the cooperatives functioning, do not create sufficient legal conditions to unify the agricultural producers, especially small business forms, for the joint cultivation of land, production, and marketing, processing, storage, supply them with material and technical resources and other types of service.

In general, the current development state of the cooperatives in both countries, regardless of their forms and types, proves their public relevance in modern conditions.

IV. RECOMMENDATIONS FOR THE NATIONAL LEGAL FRAMEWORK

According to the **Union of Consumer Cooperation of the Republic of Kazakhstan**, the Law “On Agricultural Cooperatives”, presented by lawmakers as a single law on cooperation in the agricultural sector of the country, is based on the abolition of all types of rural consumer cooperatives and agricultural partnerships and the creation of a new form of legal entity called “agricultural cooperative”.

In order to distribute profits among members of a cooperative, the creation of agricultural cooperatives in the organizational and legal form of a production cooperative is envisaged, in other words, commercial organization. This provision limits the members' rights in choosing one or another form of cooperatives and does not stimulate the process of their unification.

At the same time, the Law “On Agricultural Cooperatives” provides for extensive state support. The State development program for the agro-industrial complex of the Republic of Kazakhstan for 2017–2021 was adopted, where the creation of such cooperatives is a primary task. *However, this law is inhibited* because of the high level of distrust of agricultural producers, especially small businesses, to new structures being created, fear of losing the only means of production - land and low level of legal culture in the village, lack of awareness of farmers about the benefits of agricultural cooperatives.

When considering the other two laws in force “On Production Cooperative” and “On Consumer Cooperative”, the Union of Consumer Cooperation of the Republic of Kazakhstan considers that only the latter fully meets the principles and values of the international cooperative movement and, therefore, operates on the basis of this law and the “Law on Non-Profit Organizations”.

According to the Union of Cooperatives of Kyrgyzstan, in order to stimulate and promote the activities of cooperatives, it is necessary to:

- *include in the Law “On State Procurement” in terms of the provision to the procuring entity in evaluating tender bids, benefits for the proposed price of up to 40 percent for goods produced by an agricultural cooperative in the Kyrgyz Republic, and also for jobs up to 40 percent for offers of agricultural cooperatives compared to the offers of foreign firms, provided that domestic contractors use at least 70 percent of local labor resources, as well as at least 30 percent of local raw materials and materials. The procurement of goods from cooperatives by the direct conclusion of the contract as well.*

- *make changes to the regulatory legal acts in pastures provision, in terms of priority rights granting to agricultural cooperatives the right to receive the use of pastures;*
- *it is necessary to include into the law “On cooperatives” in terms of determination of the number and types of entities for the cooperatives formation, clarifying the concepts of dividends, cooperative payments, types of shares, the procedure for enrollment and exclusion of members and so forth.*

Considering possible recommendations for the Kazakhstan and Kyrgyzstan cooperative legislation improvement, it is necessary to emphasize the main problem of these countries. Despite the presence of various state support written in the laws, as well as various government programs adopted to support cooperatives, all this remains, basically, as a declaration of actions, and not real actions.

Thus, the main recommendation is to continuously inform the state about the problems of cooperatives locally, to familiarize the government with examples of successful cooperatives in the country, to attract international cooperative experts to meet with members of the government that influence the activities of cooperatives in one way or another.

V. CONCLUSIONS

Analysis of the laws in terms of cooperation, the results of their application suggests that the main thing is the consistency and ease of the laws application. Therefore, in those countries where there is a rather large list of laws in terms of cooperation, it may be appropriate to revise this list to eliminate collisions, repetitions or to create a single law.

At the same time it is difficult to state which approach is better - unified legislation regulating the creation and activities of cooperatives.

So far, in Kazakhstan and Kyrgyzstan, none of the legal models has become successful. There is a thought that the reason for the failure of cooperation lies not only in the legislation.

In general, these countries today are at the beginning of their long journey to a “cooperative paradise”. Long and serious work is ahead on creating a favorable legal environment for the development of cooperation, if the development of cooperatives is a priority for these countries.

Cooperatives need serious multifaceted support from the state, well-established educational and consulting activities, and the creation and development of cooperative infrastructure.

International donors, bringing advanced cooperative experience, as well as supporting the financial and logistical development of cooperatives in these countries, could play an important role in the development of cooperatives. However, very rarely donor organizations work to improve the conditions for cooperation in countries that receive technical assistance.

Concentration of international technical assistance on improving both formal and informal cooperative institutions could help open up new prospects for cooperation.

All this allows us to make a conclusion that it is necessary to further improve the cooperative legislation only if the state has a correct and accurate understanding of the goal and objectives of cooperatives for the development of the country.

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