

Secondment Arrangements in Kazakhstan – How Do They Work?

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Currently, companies are contending with the vagaries of Kazakhstan labour and tax laws. As a result many are now weighing the advantages and disadvantages of the various methods used to import foreign specialists, including secondment arrangements.

Although secondments are common place in the international oil industry, they are a relatively new idea to Kazakhstan law. This means that many of the aspects of the secondment model that are beyond question in most jurisdictions are quite often difficulties for companies looking to use a secondment structure in the Republic.

We would like to examine some of the salient issues affecting secondments under Kazakhstan law.

Exactly What Is a Secondment?

Before examining the impact of Kazakhstan law, it is useful to revisit the nature of the secondment itself. In a secondment arrangement, one company (the "Secondor") 'lends' an employee (the "Secondee") to another company (the "Client") in exchange for a fee. The Secondee remains under the employment of the Secondor during the secondment and does not become a formal employee of the Client. The usual result is that the Secondee continues to draw a salary paid by the Secondor in his or her home country.

The Secondor and the Client usually come to some agreement on the liabilities arising from the improper performance of the Secondee's duties. Although these arrangements vary from contract to contract, the Secondor is usually liable (at least to some degree) for any defects and damages resulting from the Secondee's substandard work.

In addition, the parties usually apportion the liability for damages to their respective people and equipment on a Knock-for-Knock basis. Knock-for-Knock is a standard practice utilized by oil companies and oil service companies; whereby

each is responsible for loss to its own personnel and property, irrespective of which party caused the loss.

Work Permit Considerations

We have noticed in practice that many Secondors and Clients share a common misconception that the secondment of foreign specialists obviates the need for a work permit. This is categorically not the case, and companies relying on this assumption can get themselves into a legal quagmire.

Generally speaking, a foreign specialist needs a work permit if he or she wishes to work in Kazakhstan for a period of more than forty-five (45) days per year. Unfortunately the law does not distinguish work done directly for a Kazakhstan employer from work done under a secondment. In fact, the law makes no reference to secondments at all. This means that Secondees need permits to work in Kazakhstan.

Kazakhstan law requires that the 'employer' obtain the work permit for the specialist. This creates an odd result in the case of secondments, requiring the foreign based Secondor to be liable for the Secondee's misdeeds. This could lead to legal wrangling between the Secondor and the Client in cases where the Secondee's defective work product caused a loss.

Another example relates to any inquiry that might befall the Secondee or any damage to his/her property. As we explained above, the Secondor and the Client are usually liable for damage caused to their respective personnel and property under the Knock-for-Knock principle. It is not clear how this would play out if both the Secondor and the Client formally employed the Secondee.

Finally, the use of two (2) employment contracts raises issues with respect to the Secondee's remuneration. If the Secondee is formally an employee of the Client, then should his or her entire salary be paid directly by the Client in Kazakhstan

under the local law agreement? This is another point where Kazakhstan law and the secondment model do not mesh properly. The Secondee may have legitimate concerns about being paid in Kazakhstan when he or she normally works in the UK, for instance. In any case, the Client normally pays the Secondor's fees and not the Secondee's salary.

We understand that some companies draft the local employment agreement in such a way that some amount of money is classified as salary and is paid in accordance with the terms of the secondment Agreement between the Secondor and the Client. Evidently, the allocation of salary under the local employment contract is a sensitive matter that can, if done aggressively, raise risks of tax evasion in Kazakhstan.

Corporate Tax Matters Affecting the Secondor

Under the Tax Code, income derived by non-resident companies from goods, works and services in Kazakhstan is considered to be Kazakhstan source income and is subject to Kazakhstan corporate income tax. Since the secondment of personnel generally constitutes the provision of services to the Client, the Secondor's income from the secondment agreement is usually subject to tax. In situations where the Secondor is a non-resident of Kazakhstan for tax purposes, the Client withholds the tax at source. The general rate of withholding tax is fifteen percent (15 %), unless altered by international treaty between Kazakhstan and the Secondor's home state.

One might assume that seconding an employee into Kazakhstan is enough to determine the residency of the Secondor. At first glance, the Tax Code appears to provide some relief in this respect. Under the law, the Secondor is not deemed to be a resident merely as a result of entering into a secondment arrangement; provided that the:

1. Secondee acts exclusively on behalf of and in the interests of the Client;
2. The Secondor is not liable for the results of the work performed by the Secondee; and
3. The Secondor does not have more than a ten percent (10 %) mark up on the secondment costs.

The second criterion listed above is of particular importance. As stated, the Secondor is usually liable for the actions of the Secondee, and such responsibility goes to the heart of the Secondor's

reputation as a good service provider. A Client may perceive any attempt to step away from such liability as a negative sign of the Secondor's trustworthiness.

The ten percent (10 %) mark-up limitation is similarly restrictive. In view of the commercial restrictions, the above residency exemption would not appear to be of great use for many oil service companies. From this narrow exemption, it would seem that the State is intent on pushing international service companies to register and pay taxes in Kazakhstan in respect of secondment income.

To the extent the Secondor qualifies as a resident under Kazakhstan law, its income is taxable at thirty percent (30 %). Depending on the Secondor's home country, the burden of double taxation may be alleviated by international treaty.

Personal Income Tax Matters Affecting the Secondee

The following benefits qualify as taxable source income in the hands of the Secondor in Kazakhstan:

- ! Income received from under employment and other agreement.
- ! Additional payments made for living expenses.
- ! Other benefits such as expenses for meals, housing, schooling for dependants, and expenses related to leisure activities, including vacation travel for family members.

The above categories cover not only the Secondee's salary but also any allowances and benefits paid in connection with that person's travel to, from and during their stay in Kazakhstan. The taxes in question are to be withheld at source. This is another point where Kazakhstan law does not meet the standard secondment model. Evidently, the only party in a position to withhold at source would be the Client. In any case, the Client is unlikely to make a large portion of the payments made to the Secondee. The result of the foregoing is that the Secondee must pay individual income tax on those other payments by him or herself.

On a final note, Secondees should be registered as taxpayers in Kazakhstan. This will allow for the payment of taxes and will lessen the risk of any personal liability on the employee for failing to pay taxes. Depending on the Secondee's home country, the burden of double taxation may be alleviated by international treaty. □