

CROSS-BORDER ASSIGNMENTS – TAX ISSUES

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Nowadays, many companies use cross-border assignments to enable their employees to gain international experience, access new markets, share knowledge, motivate employees, as well as for a number of other reasons. In the case of most companies, sending employees on cross-border assignments involves a range of responsibilities and complex challenges, such as the need to address the issues of migration, country-specific statutory reporting, the handling of home and host country payroll, including shadow payroll and the taxation of income. It would be fair to say that taxation is arguably one of the most complex issues in cross-border assignments.



As tax rules vary widely in different countries, respective tax considerations should be borne in mind both during planning and throughout the period of such assignments. This is particularly true for personal income tax (PIT), as individuals are often most concerned about taxes in their host country and may even be unaware of tax filing obligations in their home country, and vice-versa.

Under Kazakhstan's tax legislation, the tax treatment of individuals depends on their tax residence status. Tax residents of Kazakhstan are required to pay PIT on their worldwide income, while KZ tax non-residents only pay PIT on their Kazakh-source income. Income that an individual (both resident and non-resident) earns from employment in Kazakhstan is treated as Kazakh-source income, regardless of where this income is paid or who pays it.

Therefore, when moving from country to country, it is essential that the individual determine his/her tax residence status for a certain period, as this status plays a key role when determining the individual's personal income tax obligations in his/her home country and host country. In general, when there is a conflict between the domestic laws of two countries and both countries claim that the individual concerned is a resident of a specific country, the individual is entitled to refer to the respective double tax treaty to determine his/her tax position in each country.

Determination of tax residence status

Under Kazakhstan's Tax Code, an individual's residence status is determined by his/her physical presence in Kazakhstan for any consecutive twelve-month period in a specific tax year and by the center of vital interests (CVI) of the individual. In particular, an individual can be regarded as a KZ tax resident if he/she spends 183 days or more in Kazakhstan for any consecutive twelve-month period in a specific tax year **or** if Kazakhstan is his/her CVI. An individual is deemed to have a CVI in Kazakhstan if the following three criteria are met simultaneously:

- The individual is a Kazakh citizen or has a permanent residence permit in Kazakhstan;
- The spouse and/or close relatives of the individual lives/live in Kazakhstan;
- The individual and/or the spouse/close relatives of the individual owns/own or possesses/possess immovable property in Kazakhstan which is permanently available for the accommodation of the individual's spouse and/or close relatives.

If the above residence criteria are not met, the individual is regarded as a KZ tax non-resident and is not required to report his/her worldwide income in Kazakhstan.

Moreover, a foreign citizen can be regarded as a KZ tax non-resident based on the provisions of a respective double tax treaty. Most of the double tax treaties signed by Kazakhstan stipulate 'less stringent' tax residence rules, which might actually enable foreign citizens assigned for long-term work in Kazakhstan to continue to be regarded as tax residents of their home countries even if the above criteria stipulated by Kazakh tax legislation for a KZ tax resident are met.

However, in order to confirm their status as tax residents of their home countries and be eligible for the double tax treaty benefits in Kazakhstan, such individuals are required to submit tax residence certificates issued by the competent authorities of their home countries to the tax authorities in Kazakhstan. If such documented proof is not submitted, foreign citizens will be unable to leverage the double tax treaty benefits in Kazakhstan and will not be entitled to automatic release from the obligation to file a personal income tax return in Kazakhstan.

In view of the above, for cross-border assignments it is critical to determine correctly the residence status of an individual because the individual may in certain instances continue to be a resident of his/her home country based on the CVI or other criteria of the respective double tax treaty even if he/she spends most of the time in the host country.

Personal income tax return filing obligations

KZ tax residents are required to file an annual PIT return if during a tax year:

- They earn income that is not subject to withholding in Kazakhstan (for example, property income or foreign-source income), or
- They have property (real estate, securities, equity interests) outside Kazakhstan (this is applicable only to Kazakh citizens and foreign citizens who have a permanent residence permit).

Non-resident individuals are required to file annual PIT returns if they earn Kazakh-source income that is not taxed at the source of payment in Kazakhstan.

In addition to the above and as a response to the most common question “How will the authorities find out about my income?”, it is worth mentioning here standard practice involving the automatic exchange of information provided by a number of countries.

In 2018 Kazakhstan signed the *Multilateral Competent Authority Agreement on Automatic Exchange of Financial Account Information* developed and approved by the Council of the Organisation for Economic Co-operation and Development (OECD), but has not started exchanging financial account information, as some procedures on the assessment of privacy and data protection measures still need to be resolved. However, at present Kazakhstan can still request information on a case-by-case basis.

It is also worth noting the following administrative and criminal penalties for the failure to file PIT returns:

- The first time an individual fails to file an annual PIT return with the Kazakh tax authorities by the deadline results in the issue of a Notification by the tax authorities, while any repeated violation during the year is subject to an administrative fine in the amount of 15 times the monthly calculation index (MCI) (approximately USD 100).
- Understatement of PIT amounts in the tax return results in a fine of 10 times MCI (or approximately USD 70).
- Concealment of a taxable item gives rise to a fine of 200% of the concealed tax amount, while a similar violation repeated during the year is subject to a fine of 300% of the concealed tax amount.
- The Concealment of property outside Kazakhstan results in a fine 100 times MCI (or approximately USD 690) for each concealed reportable item, while a similar violation repeated during the year is subject to a fine 200 times MCI (or approximately US\$1,400).

A criminal fine is stipulated for large-scale tax evasion, in other words, if the amount exceeds 20,000 MCI (approximately US\$140,000). Furthermore, administrative and criminal fines may adversely affect not only the reputation of the individual, but also the company or even group of companies employing this individual. Moreover, it is not widely known that Kazakh legislation may prohibit foreign citizens from entering Kazakhstan if they failed to submit a PIT return during their previous stay when the filing was mandatory.



Impact of the COVID-19 outbreak

It is clear that the COVID-19 pandemic has not only affected the private lives of individuals, but also triggered a multitude of tax residence issues for individuals and businesses. Due to the travel restrictions imposed by countries globally, many cross-border workers:

- have relocated to their home countries (and work from home);
- have stayed in their host countries and work from their home/accommodation in their respective host country;
- have relocated to third countries (and work from a temporary accommodation); or
- have been dismissed.

All the above factors indicate a change in regular work patterns and routines, which raises several tax-related issues for cross-border workers and companies. In particular, companies are concerned about changes in the tax residence status of their employees and changes in the working patterns of cross-border workers, which might trigger a “permanent establishment” and thereby create new filing requirements and tax obligations for the companies.

Tax Residence for cross-border workers

The OECD has examined the implications of these changes against the backdrop of the current global pandemic and developed guidance. According to the guidance, in a number of circumstances it is highly unlikely that the COVID-19 pandemic will result in a change in the tax residence of employees.

Several countries are formally overlooking or “forgiving” sudden changes in the duration of cross-border assignments and residence status. Some countries (for example, the UK, Australia, Ireland) issued guidance to disregard the days spent in these countries for tax purposes in exceptional circumstances such as COVID-19. However, in some instances, the period for forgiveness is limited or is not stipulated in local tax law, as is the case with Kazakhstan.

Accordingly, there is still a risk that cross-border non-resident employees of Kazakhstan staying in Kazakhstan and unable to leave the country owing to the closure of international borders might be regarded as Kazakh residents under local tax law even if the individual is stranded in Kazakhstan (for more than 183 calendar days) due to travel restrictions and lockdown measures.

Permanent Establishment (PE)

According to the Tax Code, a PE is a fixed place of business through which a non-resident legal entity engages in entrepreneurial (i.e., income-generating) activities in Kazakhstan. Such a fixed place of business includes any place of management, branch, division, or representative office in Kazakhstan, regardless of the duration of the activity carried out through the fixed place of business. Moreover, non-resident legal entities are deemed to have a PE in Kazakhstan when they provide services/do business through employees or other hired personnel in Kazakhstan for more than 183 calendar days in any period for 12 consecutive months. In some circumstances the Tax Code also regards a dependent agent as a PE of its principal.

The national/local threshold for presence in the country that necessitates tax registration is generally lower than the one applicable under a respective double tax treaty. If services are provided in Kazakhstan through employees or other personnel (for the same projects or connected projects), the threshold under most tax treaties is limited to a period of more than 12 months. In general, in each case the employee’s presence and the nature of their work duties should be analyzed from the perspective of compliance with the above criteria in order to mitigate the tax consequences.

In the opinion of the OECD, changes in the work patterns of employees due to the COVID-19 pandemic will not result in any changes to the determination of a PE. To qualify as a PE, the activity carried out by an individual must involve a certain degree of permanency and must not be temporary

or transitory. Based on the assumption that remote work is a temporary development and does not become a permanent arrangement over time, working from home during the pandemic should not create a PE for the company.

In addition, anyone working from home temporarily for a non-resident legal entity can give rise to a dependent agent PE if the respective employee habitually concludes contracts on behalf of the legal entity. The key word in this context is “habitually.” If work from home is attributable to government directives issued during the COVID-19 pandemic, then such work would not be treated as “habitual.” However, if the employee had habitually concluded contracts on behalf of the legal entity in the home country before the pandemic, then the work from home required by the pandemic would not change the assessment.

National tax administrations are encouraged to provide relevant guidance, given that the changes caused by COVID-19 might trigger registration requirements for corporate income tax purposes. For example, the *Office of the Revenue Commissioners of Ireland* has issued guidance, stipulating that the presence of an individual in Ireland or any other jurisdiction as a result of the COVID-19 travel restrictions is disregarded during the COVID-19 pandemic for corporate income tax purposes.

As in the case of the tax residence of individuals, the *State Revenue Committee in Kazakhstan* has not issued any official guidance on how to determine a PE in the context of COVID-19. The country’s formal position is still based on local tax rules and remains unchanged: there is no specific tax procedure which takes account of the current global pandemic.

Owing to the lack of specific guidance during the COVID-19 pandemic, there are risks that cross-border non-resident employees might be treated as KZ residents and that it might be held that PEs have been created in Kazakhstan for foreign legal entities which sent employees on such cross-border assignments. Many tax professionals are aware of these risks. However, as they tend to concern a limited number of employees, they assume the risks to be manageable. In the case of a number of companies, however, the current situation could affect a far higher proportion of employees, which is leading them to prioritize this issue.

In summary, Kazakh tax law adheres in general to international tax principles on the taxation of individuals employed by global companies. However, even though international double tax treaties ratified by Kazakhstan take precedence over its domestic tax law and are implemented directly, there are still a number of situations where a conflict between domestic law and double tax treaties may arise. In practice, each case is considered on its merits. At the same time, however, in most cases domestic tax rules take precedence.