

## Astana International Financial Center: can it become a regional finance hub?

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**In May 2015, the Kazakhstan President announced a new ambitious program titled 100 Concrete Steps for Realization of Five Institutional Reforms of the Head of the State (100 Steps). The 100 Steps initiative is not only a response to the global challenges, but also a strategic plan to bring Kazakhstan into the world's 30 most developed nations. One element of this plan is the establishment of the Astana International Financial Center (AIFC). *Managing partner Aset Shyngysov and partner Bakhytzhon Kadyrov at the Almaty office of global law firm Morgan Lewis, ask whether the project has legs.***

The 100 Steps provide for the AIFC to be provided with a special status directly in the Kazakhstan Constitution, the country's supreme law, enjoying its own independent judicial system with its own jurisdiction based on English law, with the judicial corpus formed by foreign specialists. The AIFC is expected to grow into a financial hub for the Commonwealth of Independent States, West and Central Asia with the aim of becoming one of the world's 20 most advanced financial centers.

The AIFC is, the government argues a natural extension of the economy, given Kazakhstan's long-awaited accession to the World Trade Organization and the establishment of the Eurasian Economic Union among Kazakhstan, Russia, Belarus, Kyrgyzstan and Armenia. In addition, the government has adopted legislation providing investors with sweeteners, including a subsidy of up to 30% of the investment and tax holidays; and the accession of Kazakhstan to the Convention on Mutual Administrative Assistance in Tax Matters of 1988 which, *inter alia*, provides for an exchange of information among member states. These are important changes should hopefully help establish AIFC and further open up Kazakhstan.

Kazakhstan has very high expectations for AIFC, including the creation of a leading financial center for the region, with particular expertise in capital

market, asset management (including private banking) and Islamic financing; it is expected to contribute up to 1% of non-hydrocarbon GDP increase each year up to 2025 (equivalent to a turnover of \$13.4bn in aggregate between 2015 and 2025; and it is hoped it will attract approximately \$351bn in foreign investment over the intervening period into the Kazakhstan capital market, including \$91bn of sovereign bonds.

The law governing the AIFC is probably the most attractive and yet controversial element its set up. While it is evident that Kazakhstan lures investors with the “English law” concept, it remains to be seen how it will be implemented in Kazakhstan, a civil law jurisdiction. It seems the constitutional law on AIFC will be based on the same principles, norms and standards of leading international financial centres such as the DIFC in Dubai. However, terms outlined in ratified international treaties will ultimately prevail. A number of new laws and changes to various regulations have been adopted (including changes to the constitutional law governing the AIFC, a presidential decree supporting its establishment and a detailed joint government/central bank plan to help design the remit of the project.

There are four bodies in in the new financial centre: the AIFC Management Council – headed by Kazakhstan President; determines strategy and implements other strategy functions; the AIFC Administration – the main governing / operational body created in the form of a joint stock company, which has a board of directors and a management board, headed by Kairat Kelimbetov, former governor of the National Bank; the AIFC Financial Services Committee, which regulates provision of financial services; and the AIFC Court, which is an independent court not integrated into Kazakh court system (except that the enforcement will still be through normal court enforcement procedures). There will be a statute regulating AIFC Court activities which will likely be based on procedural principles and norms of English law and/or standards of the leading international financial centers. The AIFC Court will have jurisdiction over disputes between AIFC participants, AIFC bodies and their employees, disputes relating to operations conducted in AIFC or subjected to AIFC laws, and disputes directed to AIFC Court by third parties.

Technically speaking, AIFC will be a designated area within the boundaries of the city of Astana. The AIFC will be located at the Astana Expo 2017 facilities, opening at the beginning of January in 2018, and will be provided the Astana Expo 2017 premises along with an exemption from lease payments for two years. The AIFC will be multifunctional, including the legal entities registered or accredited at AIFC. It will contain an International Arbitration Center created at AIFC, though at this point, it is

not clear what additional benefits it can provide to existing arbitration platforms (both international and local). It could also include the Kazakhstan Stock Exchange and there may very well be synergy between AIFC and the new wave of privatization recently announced in Kazakhstan, which contemplates the sale (or partial sale) of some 783 companies, including Kazakhstan Temir Zholy (national railway company), KazMunayGas (national oil and gas company), Kazatomprom (national atomic company). English will be the official language.

#### *Monetary transactions*

Monetary transactions of AIFC participants will be settled in the currency chosen by the parties. This is a sizable advantage of AIFC compared with the general currency regime in Kazakhstan, whereby transactions are settled in the local currency, Tenge, unless a party to the transaction is a non-resident. Tenge, in its turn, has been recently subject to severe devaluation. The currency control regime effective outside of AIFC, such as the terms of registration of a currency transaction with the National Bank, will not apply in AIFC. This is a plus, although currency control regime in Kazakhstan is not too restrictive and is being constantly liberalised.

#### *Taxation*

The taxation regime in AIFC is based on the Kazakhstan Tax Code, subject to the following carve-outs:

- AIFC bodies are exempt from the corporate income tax until 1 January 2066 (with some exceptions);
- AIFC participants are exempt from the corporate income tax until 1 January 2066. This exemption applies to income received from the provision of certain financial services in AIFC, e.g., Islamic bank's banking services, re-insurance services, insurance brokerage services, investment management of investment funds' assets as well as financial services determined by the AIFC Management Council;
- AIFC participants are exempt from the corporate income tax until 1 January 2066. This exemption applies to income received from legal, audit, accounting and consulting services provided to AIFC bodies and AIFC participants providing financial services listed above;
- foreigners working for AIFC bodies or AIFC participants are exempt from the individual income tax until 1 January 2066 (with some exceptions);
- individuals and legal entities are exempt from individual or corporate income tax until 1 January 2066. This exemption applies to income from capital gains, dividends and interest in respect of securities listed in the

official lists of the stock exchange, capital gains and dividends in respect of shares of AIFC participants;

- AIFC bodies and AIFC participants are exempt from property tax and land tax (with some exceptions).

While the above tax exemptions are indeed quite attractive, one needs to be careful here, taking into account both the practical tax administration and tax policy considerations. First, the tax administration appears to be still enforced by the Kazakh tax authorities, albeit “jointly” with the AIFC bodies. Historically, investors have been facing significant challenges, the “form-over-substance” approach and red-tape from the Kazakh tax authorities.

Second, from the tax policy perspective, Kazakhstan used to change the underlying rules of the game often so that there is no guarantee that the above tax exemptions will be preserved as announced, e.g., Kazakhstan once introduced and then canceled the tax stability for subsoil use contracts; Kazakhstan adopted a tax code in 2001 and subsequently replaced it with a new one (indeed, the Government now plans to replace the 2008 tax code with a new state revenue code which will combine the tax and customs codes), and Kazakhstan plans to replace the value added tax with the sales tax, etc.

#### *Visa and work permit issues*

AIFC provides for a relaxed entry visa regime, e.g., possibility to obtain an entry visa at the airport (yet certain documents confirming high qualification of individuals are still required), a 5-year visa for AIFC participants’ employees. At the beginning of 2017 citizens of OECD states, UAE, Malaysia, Singapore, Monaco as well as other countries determined by the Kazakh Government will have a right to a visa-free entry up to 30 days. Equally, AIFC bodies and participants will be able to attract foreign workforce without a work permit. This is a huge advantage because normally it is quite a lengthy and bureaucratic procedure to obtain a work permit in Kazakhstan.

Despite a decent legislation framework and great ambitions, investors still do not feel quite secure in Kazakhstan. There is lack of trust in the local institutions, such as courts, tax authorities, work permit authorities, etc. and frequent changes of the law further thwart the trust. This may conceivably was one of the reasons for (at least formal) the creation of the special AIFC legislation. Notably, Kazakhstan already made an effort to create a regional financial center, the so-called Regional Financial Center Almaty or RFCA, which, with seemingly smaller ambitions, has failed.

The AIFC, the Government and other stakeholders need to undertake enormous joint efforts to make this project happen and achieve the announced goals. A lot will depend on the political will, financial environment in the region and in the world, as well as the Government's determination and ability to significantly improve the general investment climate in Kazakhstan.

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