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Development of automotive component production business in cooperation with foreign companies

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International Forum on development of cooperation and organization of industrial suppliers business in Russia

General forms of cooperation with foreign partners in automotive business

- Distribution contract
- Purchase of automotive components/ spare parts performed by TIER1 automotive components manufacturers from TIER 2 / TIER 3 automotive components local manufacturers
- Contract manufacturing/ assembly facilities
- Sale of business/ a share in business to a foreign partner
- Establishment of a JV/ strategic alliance with foreign partners

Contract manufacturing / assembly
Key tax issues

- Necessity of modernization of production facilities/ purchase of foreign equipment to start working with a foreign partner – assessment of possibility to apply tax and customs concessions
- Structuring of intellectual property rights transfer - ?
- Possibility of funds attraction from foreign partners and effective structuring of financial flows - ?

Sale of business / share in business to a foreign partner (1/2)
Tax issues related to the "pre – sale" stage of the deal

- Tax risk assessment and identification of risk minimization options (e.g. due diligence of the sold company from the buyer's perspective - "vendor due diligence")
- Assessment of the effectiveness / transparency of the existing business structure, its attractiveness to potential investors => identification of pre-sale restructuring possibilities
- The main directions of pre-sale restructuring:
  - Protecting the rights / interests of business owners;
  - Improving the structure controllability / transparency of financial flows / attractiveness to investors;
  - Achieving the optimal level of tax burden upon profit distribution / sale of business;
  - Identification of opportunities to use international structures;
  - Negative tax history.
- Selection of the optimal transaction structure and discussion of its options with a potential buyer
- Review of the basic conditions of a sale contract and negotiation thereof with a potential buyer

Sale of business / share in business to a foreign partner (2/2)
Frequently issues raised within tax due diligence

- Tax audits and litigations
- Opaque tax history (aggressive tax minimization schemes, unrecorded business transactions in official reports)
- Scrutiny of intragroup transactions, in particular, low-tax/ offshore operations
- Use of transfer pricing mechanisms (cross - border transactions, sales of funds/ companies)
- Application of regional / local tax concessions / use of subventions
- Structuring of transactions in low-tax/ offshore jurisdictions
- Income repatriation mechanisms

NB! Tax risks could significantly affect the price of the transaction and, in principle its possibility

Typical issues related to strategic alliance (joint ventures) establishment between Russian and foreign partners

1. Identification whether the need in corporate restructuring and vendor due diligence exists before establishing an alliance / a joint venture (hereinafter - JV)

2. Elaboration of conditions of Partnership agreement / sale contract / JV agreement / shareholders agreement, etc

3. Development of an optimal joint business structure with regard to foreign partner's interests, assessment of structuring opportunities in foreign jurisdictions

Optimal joint business structure with regard to foreign partner's interests

- Assessment of the necessity to create a new holding and operating companies
- Definition of holding company jurisdiction for the purposes of tax burden optimization and improvement of business structure effectiveness
- Structuring of the parties' contributions to the JV, investigation of tax implications
- Development of an effective financial structure - especially in case of potential additional investments to the JV (optimization of interest expenses deductibility, application of "thin capitalization" rules, etc)
- Structuring of ownership / transfer of intellectual property rights
- Transfer pricing issues - ?
- Determination of key stakeholders' functional roles regarding the basic business activities, and development of efficient operational structure
- Tax aspects of operating activities and the contractual relationship between the partners (including issues related to the distribution of the profit from operational activities)
- Preliminary study of issues related to JV contract termination/ cease of participation in JV

Opportunities in Russian regions – possible tax concessions for investors

- One of the investment effectiveness criteria is a possibility to obtain investment/regional tax concessions and/or other form of state support provided on the regional level
- Administrative and declaratory orders of tax concessions provision are stipulated
- In general, tax concessions are provided for a period of 3-5 years or for the actual payback period of the investment project
- The following features related to possibility of tax concessions receipt should be taken into account:
  - ✓ priority sectors / regional investment programs that the investment project must comply with;
  - ✓ additional obligations imposed on the investor (infrastructure construction, roads) -?;
  - ✓ requirements for the minimum investment amount;
  - ✓ limitations for assets disposition/ transfer of investment funds during the period tax concessions applied;
  - ✓ requirements for absence of debts payable to the budget during the investment project period / tax concessions application period;
  - ✓ investment terms (e.g., from certain year, or during 3-5 years);
  - ✓ requirements for business plan provision / preliminary approval of the project by the regional authorities - in case of administrative order.

Opportunities in Russian regions – examples of regional tax concessions

Criteria	Level of tax concessions							
	Federal	Regional tax concessions (several regions with high concentration of automotive business as examples)						
	Special economic zone (116-FL)	**St. Petersburg** : Law 81-11 dated 14.07.1995	**Leningrad region**: Law № 113-oz dated 29.12.2012	**Kaluga region**	**Tatarstan Republic**	**Ulyanovsk region**	**Samara region**	**Nizhny Novgorod region**
Order of application	Requirement of agreement conclusion with SEZ administration	Declaratory	Administrative (Permissive)	Administrative (Permissive)	Administrative (Permissive)	Administrative (Permissive)	Administrative (Permissive)	Administrative (Permissive)
Possible tax concessions	**Profit tax** Reduction of the rate 4,5% -18% off **Property tax, land tax** (exemption)	**Profit tax** ↓ 4,5% off (15,5% rate instead of 20%) **Property tax** (exemption)	**Profit tax** ↓ 4,5% off (15,5% rate instead of 20%) **Property tax** (exemption)	**Profit tax** ↓ 4,5% off (15,5% rate instead of 20%) **Property tax** (full exemption or partly)	**Profit tax** ↓ 4,5% off (15,5% rate instead of 20%) **Property tax** (exemption or application of 0,1% rate)	**Profit tax** ↓ 4,5% off (15,5% rate instead of 20%) **Property tax** (0% - 1.1%)	**Profit tax** ↓ 4,5% off (15,5% rate instead of 20%) **Property tax** (exemption)	**Profit tax** ↓ 1% - 4,5% off **Property tax** (exemption or application of 0,55%-1,65% rate)
Period of tax concessions application	While resident status is applicable Property tax – 10 years; land tax – 5 years	5 years 7 years for profit tax (in terms of minimum investment amount of 15 billion RUB)	4 – 8 years depending on volume of investments and type of business activity	1 – 7 years (inclusively) depending on volume of investments	up to 7 years (up to 13 years regarding the projects in the machinery manufacturing industry)	Profit tax: 5 – 15 years (inclusively) Property tax: 5 – 15 years (inclusively)	4 – 7 years depending on volume of investments	5-7 years (inclusively) Depending on type of investment project
Investment amount	For residents of industrial production SEZ– minimum amount is RUB 120 mln.	Minimum amount is RUB 800 mln.	Minimum amount is RUB 50 mln. (for some districts) RUB 300 mln. (for other districts)	Minimum amount is RUB 100 mln.	Minimum amount is not stipulated	Minimum amount is RUB 200 mln.	Minimum amount is RUB 100 mln. (for profit and property tax concessions application)	Minimum amount is RUB 100 mln.

KPMG in Russia and the CIS

- more than 20 years in Russia
- 7 countries, 19 offices
- over 3,800 professionals
- part of KPMG Europe LLP, largest accounting firm in Europe
- 19 countries, 143 offices, over 32,000 professionals

KPMG in Russia

No.1 Audit Firm
in Russia

2009–2012 гг.

No.1 Audit &
Advisory Firm
in Russia

2011 г.

KPMG's Valuation team: Winner of the Big Consulting'12 Award in the Public Opinion nomination

2012 г.

Tax Firm
of the Year
in Russia

2012 - 2013 гг.

European Energy
Tax Team
of the Year

2011 г.

Audit Company of the Past 5 Years by Financial Elite of Russia Awards

2010 г.

Best Reporting
Accountant

2010 г.

No.1 Reporting Accountant in Russia by number of transactions and overall value

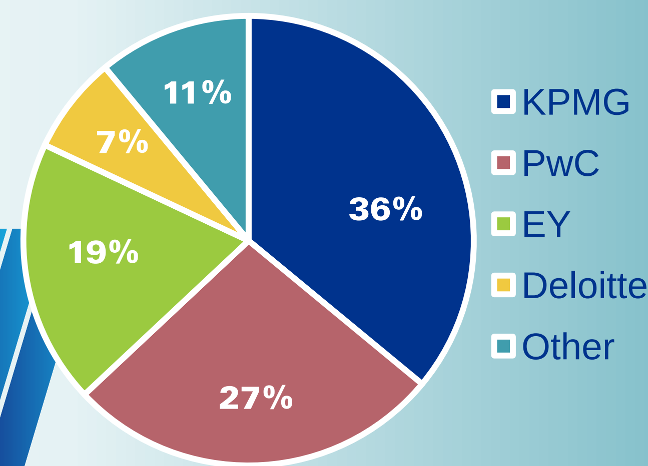
2010 г.

Insolvency
Advisory Firm
of the Year
in Russia

2010 г.

Audit market share – Top-100 Russian companies*

#1 Audit firm



** Source: Expert-400 Rating, 2013*

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