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Skolkovo Innovation Center

Tax Flash Report

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Federal Law "On Innovation Centre Skolkovo"

On 28 September 2010, Russian President Dmitry Medvedev signed the Law on the Skolkovo Innovation Centre [1](the "Centre") as well as amendments to existing legislation in connection with the adoption of the new law[2].

Participants in the project will enjoy significant benefits, including tax benefits. It makes sense for companies engaged in research activities to closely examine the advantages of participating in the project, as well as the required conditions for becoming a project participant.

What type of research will take place at Skolkovo?

The Centre will host research work in the following areas:

- ❑ Energy efficiency and energy conservation, including development of innovative energy technologies;
- ❑ Nuclear technologies;
- ❑ Aerospace technologies, primarily in the area of telecommunications and navigation systems (including building associated ground infrastructure);
- ❑ Medical technologies – developing equipment and new medications; and
- ❑ Strategic computer technologies and software programs.

The research work conducted by project participants will extend to commercializing and bringing the results of their research to market.

How will the research Centre be organized?

A management company will be responsible for carrying out the project. Toward that end, the management company will receive land as property, which will then be leased out to individual project participants. The participants will not be allowed to sub-lease their land plots.

In addition to a number of other functions, the management company will oversee approving the roster of project participants, and developing and implementing the project's bylaws and regulations (including rules for placing advertisements within the Centre). Non-compliance with the project's rules and bylaws will entail civil, administrative and even criminal liability.

The Centre's development plan also calls for creating a social infrastructure including medical and educational facilities. As well, a number of federal agencies will have field offices at Skolkovo, including the customs, tax and immigration services as well as defence, registration and insurance bodies.

[1] Federal Law No. 244-FZ "On Innovation Centre Skolkovo"

[2] Federal Law No. 243-FZ On Amending Certain Legislative Acts of the Russian Federation following the Enactment of the Federal Law On Skolkovo Innovation Centre.

Who can participate in the project?

To become a participant, you must:

- ❑ Have the status of a Russian legal entity
- ❑ Have an established executive function operating within the Centre (this criterion will apply only from 1 January 2014);
- ❑ Indicate in your incorporation documents that the sole objective of your company's operations is to conduct research work within the Centre; and
- ❑ Take responsibility for conducting research work in accordance with the Law on Skolkovo and comply with all project rules and bylaws.

Project participant status will be granted for a 10-year term.

What's the process for recruiting foreign employees?

Employers who recruit foreign nationals to work at Skolkovo do not need to obtain a permit for employing foreign workers.

Moreover, invitations for such foreigners to enter Russia will be issued through the management company independently of the regular work visa quota system.

What tax benefits will the Skolkovo project offer?

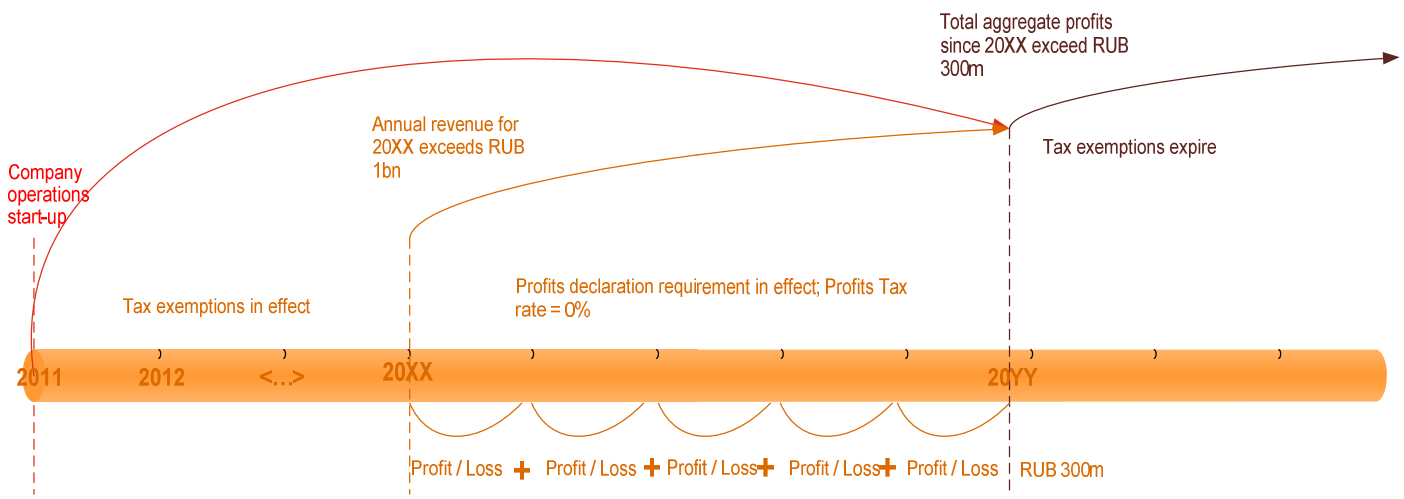
Project participants will enjoy significant tax benefits. The primary benefits are:

- ❑ Exemption from Profits Tax;
- ❑ Exemption from the taxpayer's VAT obligations;
- ❑ Exemption from Property Tax; and
- ❑ Reduced rates for mandatory insurance contributions to the Russian Pension Fund (14%), the Social Insurance Fund (0%), the Federal Mandatory Medical Insurance Fund (0%) and the Regional Mandatory Medical Insurance Fund (0%).

These benefits will be granted for a term of **up to 10 years** from the date an entity obtains project participant status, with all applicable restrictions factored in (see Figure 1 below). However, the tax benefits provided for under the Law do not extend to the management company's operations.

The Law also requires that a project participant declare its profits and losses from the first day of the year in which its annual revenues exceeded RUB 1 billion. In this regard, the prevailing Profits Tax rate from that date will remain 0% until the project participant's total aggregate profits for prior years exceed RUB 300 million. The project participant will lose eligibility for the tax benefits (exemptions) starting from the year when its total aggregate profits exceed RUB 300 million (see Figure 1 below).

Figure 1. Restrictions on tax exemption applicability



A project participant may also become ineligible for the tax benefits (exemptions) outlined above if it loses its project participant status.

Project participants may voluntarily apply Profits Tax and VAT exemptions and are entitled to discontinue using them at any time. But, if a project participant discontinues using these exemptions, such tax benefits will not be granted again.

What customs benefits will the Skolkovo project offer?

The Law allows for the refund of customs duties and VAT expenses incurred when importing into Russia goods intended for use in the construction, equipping or technical outfitting of real property facilities within the Centre, or goods necessary for conducting research work within the Centre.

Such expenses will be refundable not only for project participants but also for all legal entities and individual businesspeople **participating in the project's implementation**. [3]

What are the accounting rules?

Project participants will be exempt from maintaining accounting records. However, this exemption will be valid only if a project participant's annual revenue from the sale of goods (work, services) does not exceed RUB 1 billion.

In any case (i.e. independent of the revenue volume), project participants must maintain tax accounting of income and expenses in line with the required procedures for entities eligible for the simplified taxation system (under Russian Tax Code Chapter 26.2).

What you should expect at this stage

We assume that the Centre's internal functioning will undergo further development and fine-tuning. That said, however, the fundamental framework for how Skolkovo will operate has been spelled out directly in the text of the relevant legislation. Thus, we believe that it's already possible today to fully rely on this legal framework in weighing the pros and cons of participating in the Skolkovo project.

If your company is already conducting or plans to conduct research work in one or more of the Skolkovo Innovation Centre's priority areas, we would be happy to work with you to closely analyze and consider all the relevant issues.

[3]Under Law 244-FZ, these entities are: the management company, the management company's subsidiary, a participant in the project, another legal entity or self-employed entrepreneur engaging in the project implementation based on contracts with the management company, the management company's subsidiary, a participant in the project, except for the government body, a local self-government and an individual engaging in labour activities within the Centre.

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