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**Skolkovo – Road to Innovations**

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# Implementing Innovative Projects in Skolkovo: Legal Aspects

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# Introduction: What Is Skolkovo?



- ***Geographic Skolkovo:*** Skolkovo is the (future) hi-tech hub near Moscow run by a non-profit organization – the Skolkovo Foundation. Skolkovo will provide modern research infrastructure, friendly legal and regulatory environment, tax and customs exemptions and other incentives to its residents
- ***Virtual Skolkovo:*** Operations in Skolkovo are planned to commence not earlier than 2014. Therefore Skolkovo will operate in a “virtual” mode until 2014: any Russian corporation may participate in the project regardless of its place of residence providing it meets participation requirements
- ***Off-shore Skolkovo:*** Skolkovo will be an inner off-shore operating, to a certain extent, under its own regulations that may be quite different from those governing the rest of the country. This will be the case, inter alia, in respect of taxation, construction, employment of foreign nationals, medical care, technical regulation, education and other areas

# Introduction: Why to Take Part?



- ***Relatively friendly environment:*** Residents of Skolkovo will enjoy non-bureaucratic environment, modern R&D, business and living infrastructure and significant fiscal benefits. Sufficient local high-qualified workforce is available, particularly in IT sector
- ***Government relations consideration:*** Modernization is the declared priority of the Russian government's policy, and Skolkovo is one of the most ambitious projects of President Medvedyev. For large foreign businesses, participating in the project is a way of contributing to the environment and thus securing their market share in the principal areas of interest in Russia
- ***Secure legal structuring:*** Possibility of off-shore corporate structuring, outsourcing part of the R&D back abroad, protecting initial IP and IP generated as a result of the R&D program, etc.

- Federal Law No. 244-FZ “On Innovation Centre “Skolkovo”(the “Skolkovo Law”) dated September 28, 2010
- Federal Law No. 234-FZ “On Introduction of Amendments to Legislative Acts of the Russian Federation in Connection with adoption of the Law on Innovation Centre “Skolkovo” dated September 28, 2010
- According to the Skolkovo Law, a wide range of matters pertaining to the Skolkovo project shall be governed by regulations adopted by the Skolkovo Foundation (project rules, participation requirements, admission procedures, etc.)
- Regulation on Awarding and Cancellation of the Status of a Participant of the Skolkovo project (adopted by the Skolkovo Foundation on December 6, 2010)
- Regulations on Expert Boards, Investment Committee, the preliminary examination (all adopted by the Skolkovo Foundation in December 2010)

- According to the Skolkovo Law, only R&D projects in one of the five specific areas may be implemented in Skolkovo. These areas include “*strategic*” computer technologies and software (and space technologies including telecommunication and navigation systems)
- Declared priority areas of the Skolkovo IT and Computer Technologies Cluster include:
  - next generation multimedia web search engines;
  - recognition and editing of video and audio content;
  - analytical software;
  - integrated management systems;
  - WebX.0;
  - complex engineering solutions;
  - new communication and information storage technologies;
  - cloud computing;
  - green IT;
  - software for finance and banking industries;
  - information security technologies;
  - IT in pharma;
  - wireless sensor networks;
  - IT in education.

- **Taxation:**
  - profit tax, VAT and property tax exemptions (applicable as long as the participant's revenues and net income do not exceed threshold values set forth in the Tax Code);
  - reimbursement of customs duties and VAT paid on importation of goods for the purpose of the construction and equipping of real estate facilities in Skolkovo (applicable if the Skolkovo Foundation acts as a customs broker for the importing participants);
  - reduced pension insurance rate (14%) and exemption from statutory payments to the Obligatory Medical Insurance Fund and the Social Insurance Fund of the Russian Federation;
- **Facilities:** Project participants may use Skolkovo infrastructure (including lease of office space) on preferential terms that will be defined by the Skolkovo Foundation



- ***Employment of foreign nationals:*** A relatively liberal regulatory regime will apply to the employment of foreign nationals by Skolkovo participants. In particular, project participants are exempt from the requirement to obtain state permit for the hire of foreign nationals. The Skolkovo Foundation will act as a middleman between business and state in certain immigration matters, etc.
- ***Relaxed regulatory regime:*** Non-bureaucratic environment. Some state and municipal functions are carried out by the Skolkovo Foundation. Interactions with public authorities will be facilitated by the setting up of departments at such authorities specifically responsible for Skolkovo
- ***Financing:*** The Skolkovo Foundation, through special seed funds, may provide financing to start-ups and other project participants.
- ***Accounting:*** Smaller businesses are exempt from the requirement to keep accounts in compliance with the Russian law on bookkeeping.

# Participation Requirements



- Incorporation in Russia
  - The Skolkovo Law and applicable regulations of the Skolkovo Foundation do not provide for any restrictions on foreign control. Thus, a wholly owned subsidiary of a foreign company may also apply to become a participant
- Residence at Skolkovo (applicable from 2014)
  - This requirement does not prevent participants from having branch offices on other locations
  - Companies applying for the status of participants now will have to move their headquarters to Skolkovo by 2014
- The constitution documents of any participant may allow solely the carrying out of research and development and related activities in the areas set forth by the Skolkovo Law
  - Within the meaning of the Skolkovo Law, “research and development” includes commercialization of their yields. It is not yet clear what “commercialization” is intended to mean in this context. Apparently this requirement will mean that the participant may not engage in production and trade activities, but may e.g. license products out to third parties including the participant’s shareholders

- Assumption of the obligation to carry out research and development within the meaning of the Skolkovo Law in compliance with the rules adopted by the Skolkovo Foundation
- The applicant for the participation status shall plan implementing a project that:
  - (i) is within the specific areas of research set forth by the Skolkovo Law;
  - (ii) involves the development and/or commercialization of unique and/or globally competitive products and/or technologies; and
  - (iii) involves the participation of a foreign specialist with a high reputation in investment and/or research community (such specialist to declare his consent to participate in the project)
- A specialist carrying out academic activities at a Russian or foreign university or research institution must participate in the project presented by the applicant (such specialist to declare his consent to participate in the project)

- Admission procedure is governed by the Regulation on Awarding and Cancellation of the Status of a Participant of the Skolkovo project
- The Skolkovo Foundation has the authority to grant and cancel participant status
- A corporation assumes the participant status as of the date of its entry in the Register of Participants of the Skolkovo Project
- Applications are made by completing the form on the Skolkovo Foundation's website. The applicant must, among other things, provide details of the planned R&D project. Any application goes through formal and substantive examination process. The latter is not carried out if the project at issue went through the optional preliminary examination and was approved
- Substantive / preliminary examination is carried out by an independent expert board
- Participation in the project (and any benefits that go along with it) is limited to *10 years* from the date of registration

- The Skolkovo Law and the Regulation on Awarding and Cancellation of the Participant Status provide for specific circumstances whereby a participant may be expelled before the expiration of the 10-years period. These include:
  - violation of the Skolkovo Law by the participant
  - violation of the project rules adopted by the Skolkovo Foundation
  - refusal of the participant to participate in the project
- The law does not set forth any materiality threshold in respect of the violations that may lead to the dismissal. Thus, theoretically even minor incompliance may result in the cancellation of the participant status
- In particular, conducting any activity other than research and development in the relevant areas and related activities is regarded as the violation of project rules and may lead to the cancellation of the participant status

- Joint venture with a Russian partner...
  - ... with or without the licensing of the initial IP by the foreign investor
  - ... with the JV company conducting the R&D program and owning any new IP that may be generated as a result
- OR
- ... the JV company conducting the R&D program as a contractor for the foreign shareholder on the basis of an R&D agreement *or vice versa*, with newly generated IP being “distributed” between the foreign shareholder and the JV company
- Participating in the project through a wholly owned Russian subsidiary
- Outsourcing research and development to a Skolkovo participant without having equity participation in it
- Venture investments
- M&A: acquisition of indigenous Skolkovo start-ups

# Structuring a Skolkovo JV

- ***Corporate structuring:***
  - off-shore or on-shore, choice of jurisdiction
- ***Financial structuring:***
  - providing equity and/or loan capital
  - attracting funding from Skolkovo or state-controlled capital providers
  - impact on corporate structuring: financing SPVs parallel to holding SPVs
- ***Contract structuring:***
  - using R&D contracts between shareholder(s) and the JV company to make enforceable arrangements in respect of future IP, to direct cash flows, etc.
  - outsourcing part of R&D to other Russian and/or foreign companies
- ***Intellectual property:***
  - Initial IP licensed to the JV company: license structure, protection of IP
  - New IP generated by the JV company: control, distribution, IP protection
- ***Other issues:*** supervision of the R&D program, staffing, etc.

- *On-shore structuring:*
  - Russian JV company, Russian corporate law
  - lack of flexibility and uncertainties in respect of internal structuring of the joint venture (e.g. Russian law shareholders agreement)
  - exclusive jurisdiction for corporate disputes under Russian law, risk of non-enforceability of arbitral awards
- *Off-shore structuring:*
  - off-shore JV company, Russian project company
  - greater flexibility in corporate and contract structuring
  - less enforcement risks
- Some large Russian companies, especially state-controlled, insist on using on-shore structures despite their inherent inflexibility and uncertainties
- HoldCo, FinCo



- ***Initial intellectual property:***
  - the R&D program may be conducted on the basis of existing IPR (software copyrights, know-how, patents, integrated circuit layouts)
  - various structuring options: license, contribution of a license or exclusive rights into the charter capital, establishing an IP SPV – contribution of its shares, pledges, licenses, etc.
  - key risks include: losing of corporate control over the JV or project company holding IP rights, unlawful use of contributed IP (e.g. know-how) by the JV company or the JV partner for non-authorized purposes, etc.
  - sometimes initial IP is the only major contribution of the foreign partner
- ***IP generated by R&D:***
  - the foreign JV partner is usually interested in having direct control over the “new” IP
  - in many cases Russian law makes it difficult to make enforceable contractual arrangements in relation to future IP (such as are usual in foreign JV and shareholder agreements)
  - therefore: importance of proper contract structuring (e.g. by way of R&D agreements whereby the JV / project company may be acting as the contractor OR the client)
  - in “IP-driven” joint ventures, it is possible to secure the foreign shareholder’s rights in initial IP and interests in future IP even if that shareholder does not have corporate control over the JV company
  - appropriate contractual arrangements with the employees of the project company are highly important (work-for-hire issues)

- Software copyright
- Invention patents, utility models
  - patentability of software-based solutions
- Know-how (trade secrets)
  - rigid formal requirements to the confidentiality regime. Risks relating to the protection and licensing of know-how owned by foreign companies
  - proposed amendments to Russian know-how law
- Integrated circuit layouts
- Licensing: VAT exemption on patent and software license agreements
- Use of foreign law in IP license and assignment agreements

- Skolkovo provides comfortable legal and regulatory framework and an attractive tax regime for R&D in Russia, as well as an opportunity to contribute to the environment and send a positive signal to the government
- There are no limitations on foreign businesses to participate in the project and avail themselves of the Skolkovo benefits
- Foreign businesses can participate in a number of different ways. Flexible corporate structures are available to secure investments
- Appropriate contract structuring allows protecting IP owned and contributed by the investor and making enforceable contractual arrangements in respect of future IP yielded by the R&D program
- The enforcement of intellectual property laws is improving steadily. Russian law provides sufficient IP protection and tax exemptions for certain technology transactions

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# Thank you!



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Thank you!

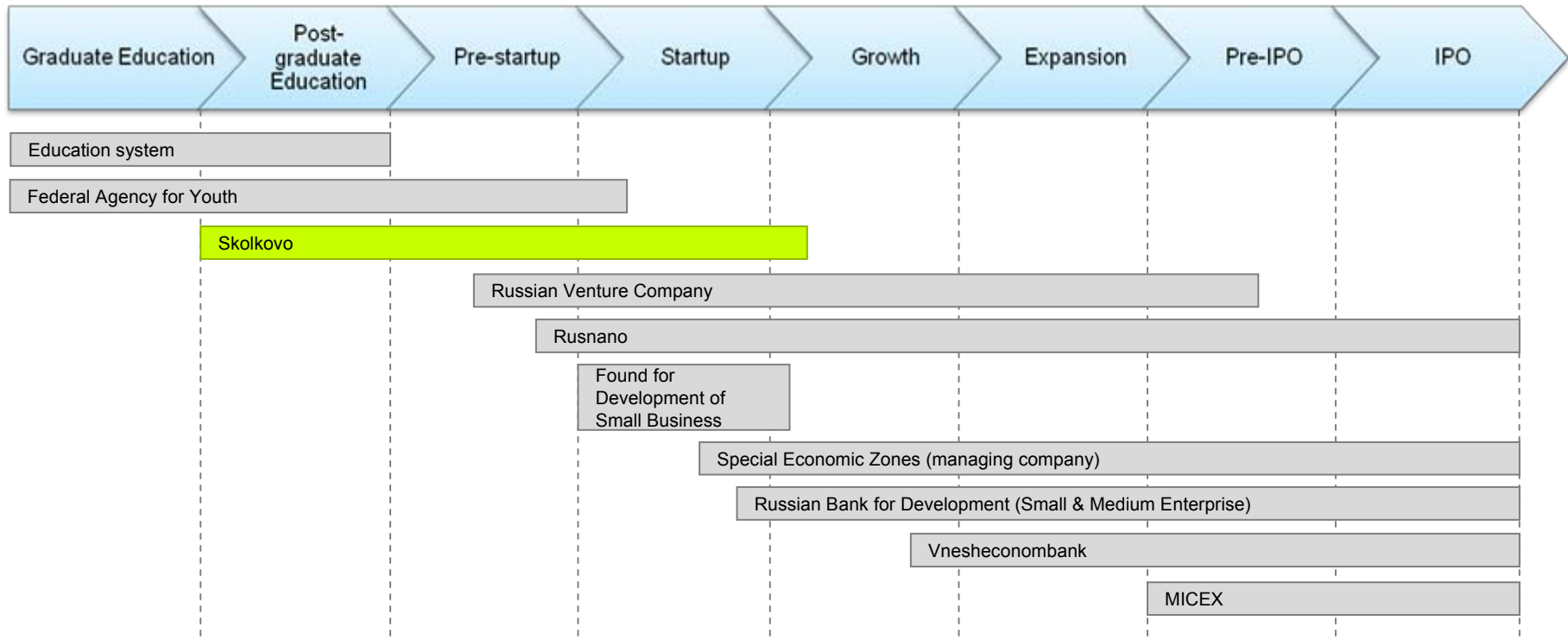
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## **SKOLKOVO.**

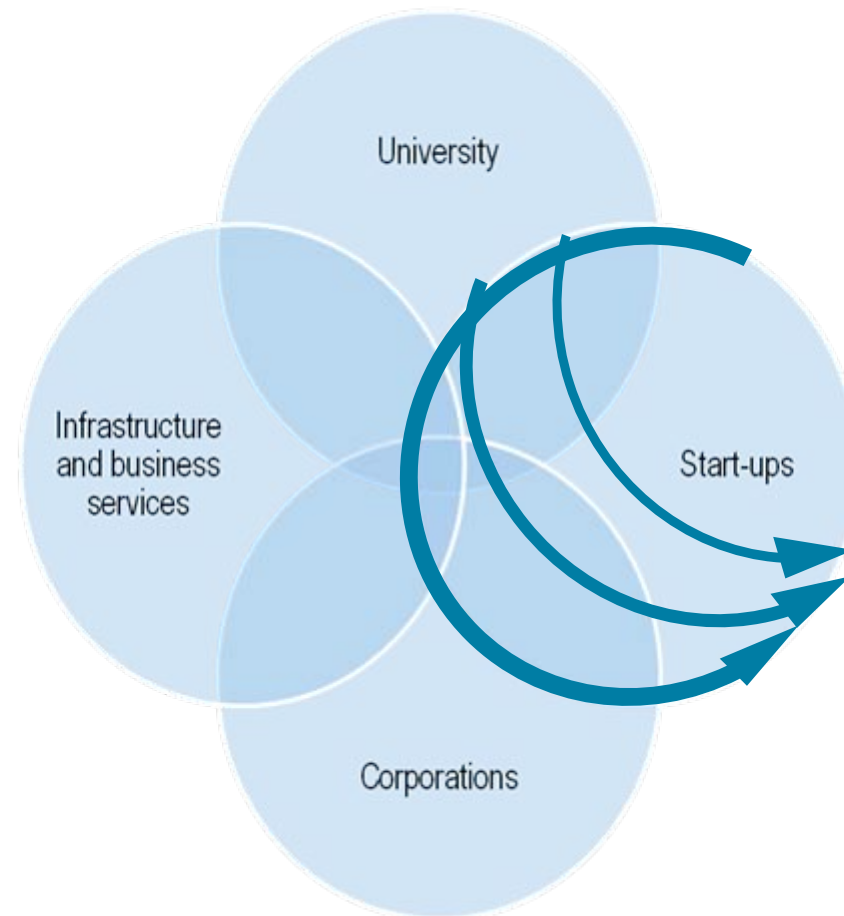
- Innovation infrastructure in Russia;
- Skolkovo concept;
- Cooperation model with major corporations;
- Start-up activity status.

All phases of the innovation life-cycle are covered by the existing “development institutes” in Russia from an idea conception till listing on stock exchange. At the moment cross-organizational cooperation model is being structured through a number of multilateral arrangements.

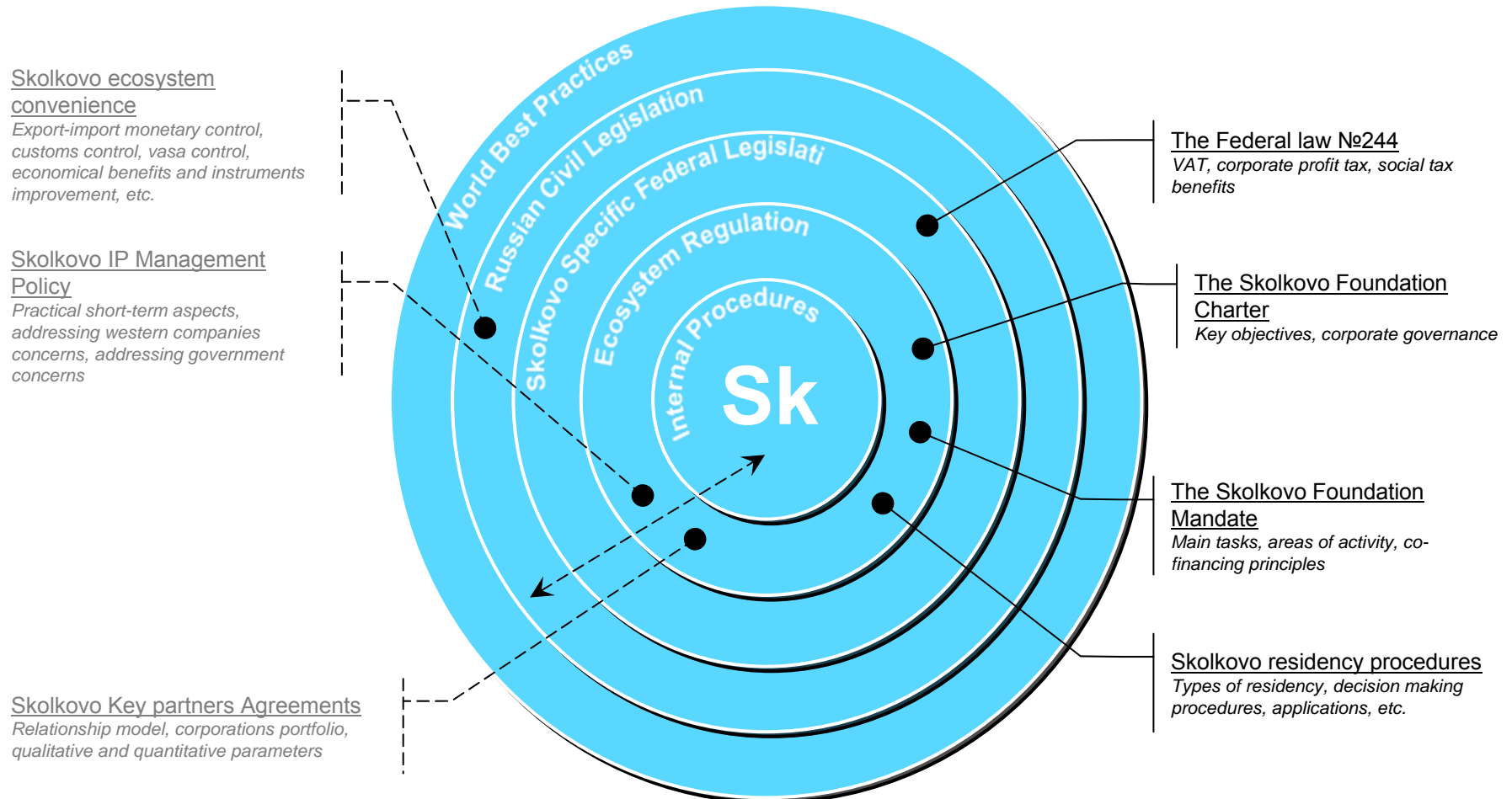




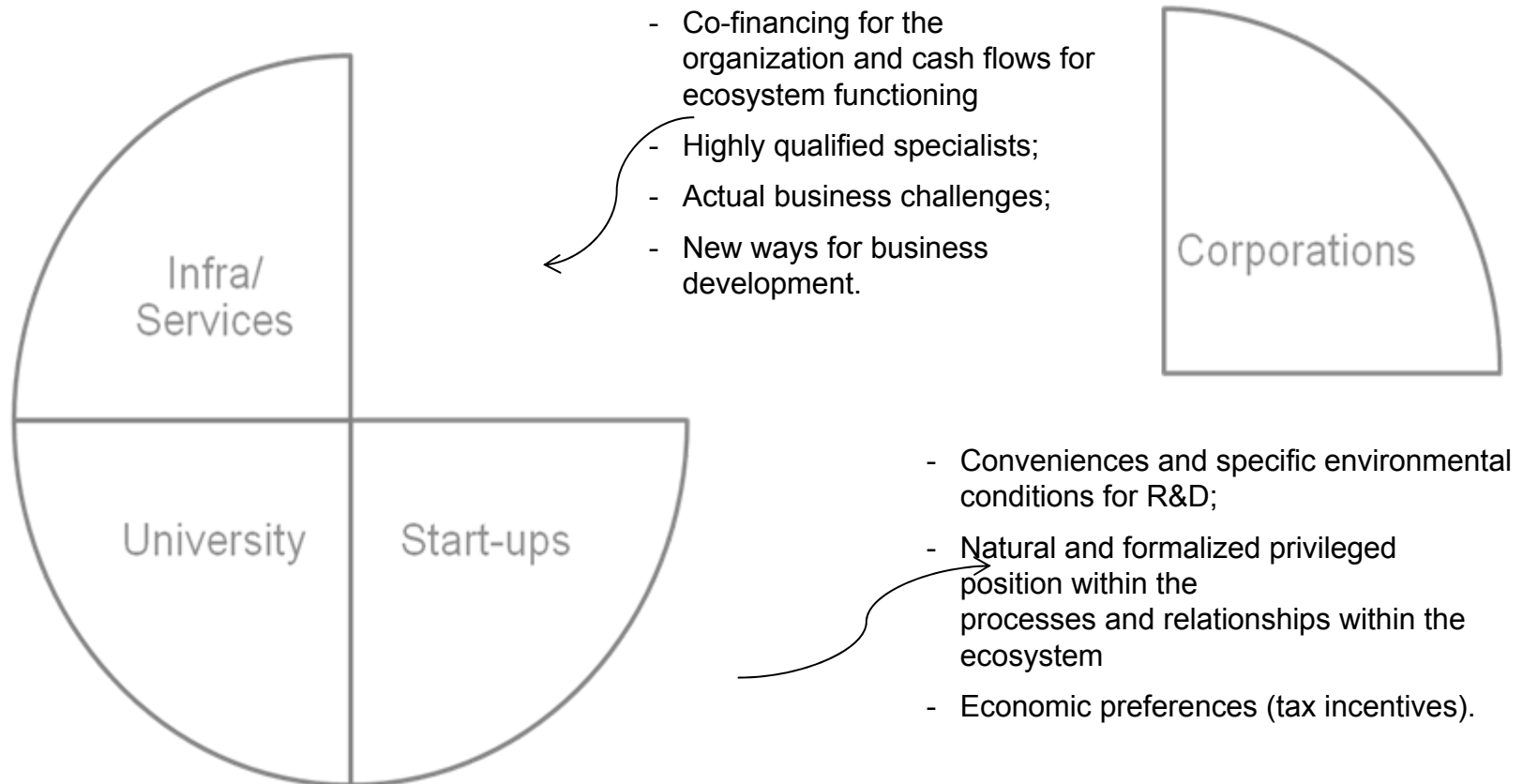
Key objective of the Skolkovo project refer to maximization of startups through structuring ecosystem offering all innovation accompanying elements/activities.



Skolkovo has been created through federal law №244 introducing number of tax benefits for Sk residents. Development of large volume of ecosystem and procedures related regulation will be undertaken is being undertaken and will proceed through 2011. More importantly, number of legal initiatives and policies (e.g. Skolkovo IP Policy) will be developed and initiated in 2011.

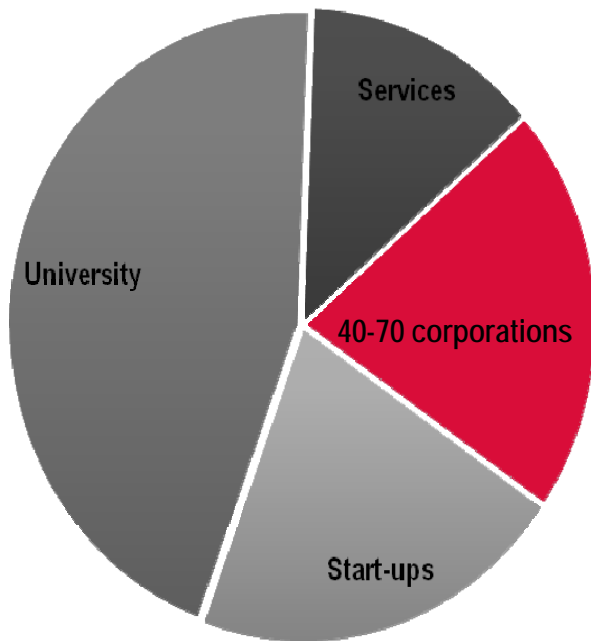


Portfolio of corporations, that are physically presented in Skolkovo, *should* provide a critical mass of demand and supply in various forms at all levels of the ecosystem, receiving in return an *equivalent* amount of a service / preferences / options.

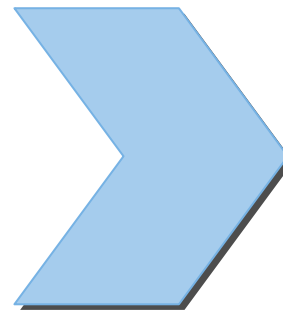


Skolkovo key partner status related benefits, portfolio vision and selection approach procedure will be documented in the respective Skolkovo policy to be drafted, publicly discussed and approved through the year 2011.

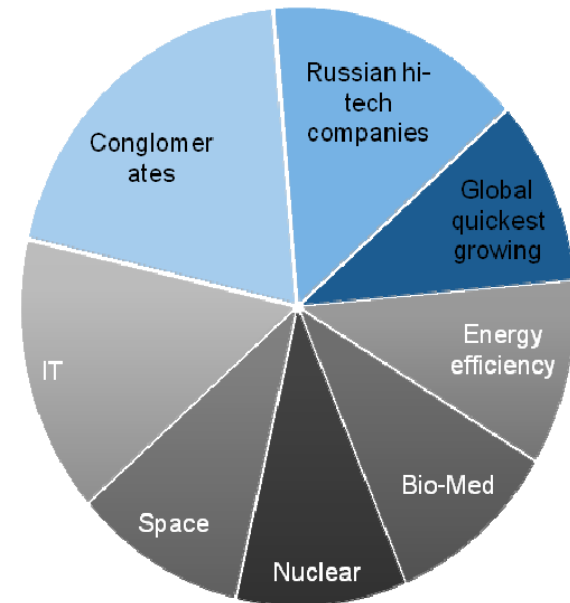
## Skolkovo City Vision



**Total 20 625**  
residents



## Corporate Presence Structure Vision



**Total 40-70**  
companies

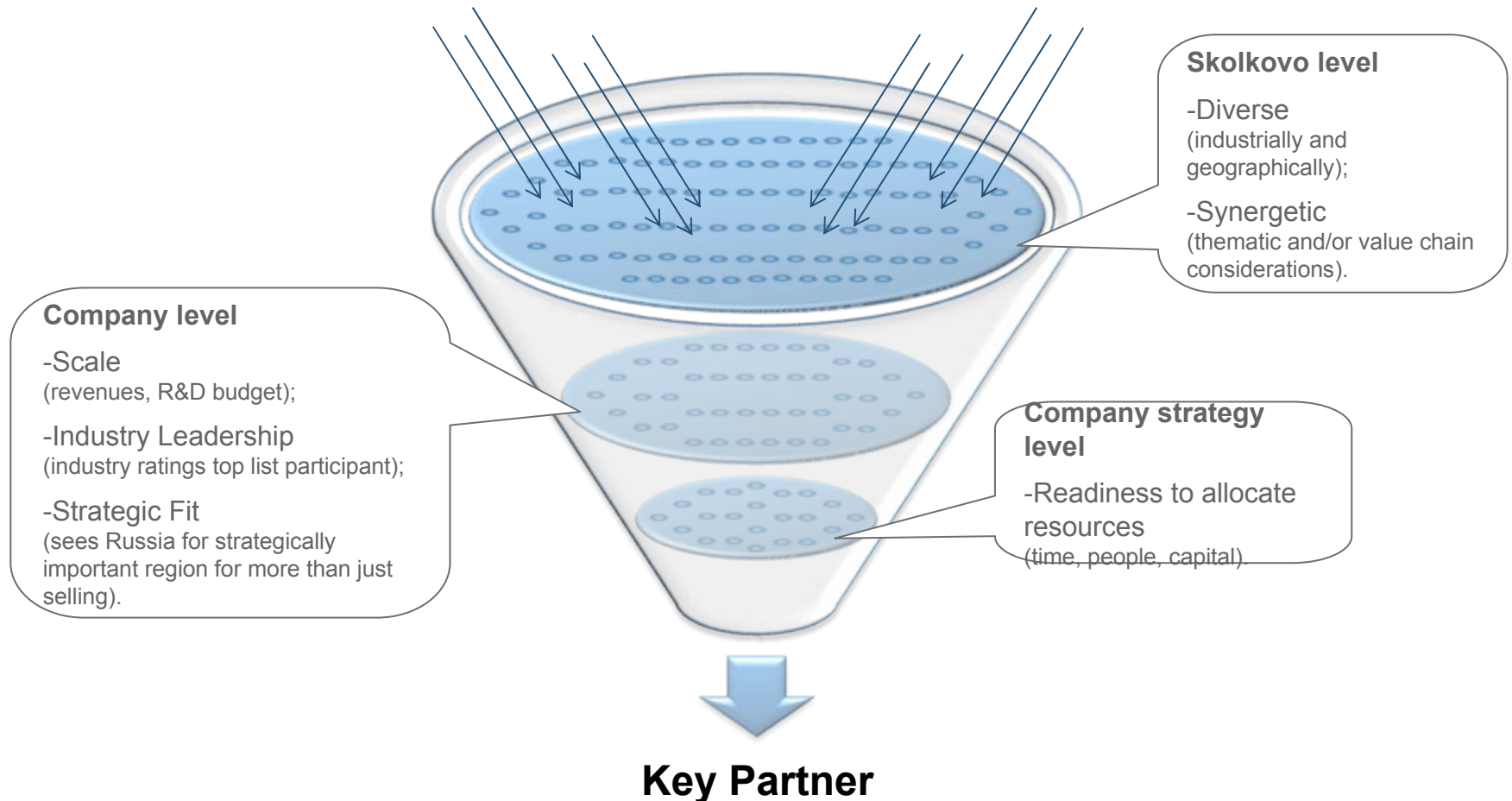
**2000**  
researches

Four types of companies are seen to be represented at Skolkovo: (i) world leading conglomerates carrying out R&D in numerous areas, (ii) medium-size companies – global growth leaders, (iii) one industry specialized technological leaders and (iv) Russian high-tech companies.

## Target structure of the Skolkovo Key Partners Portfolio



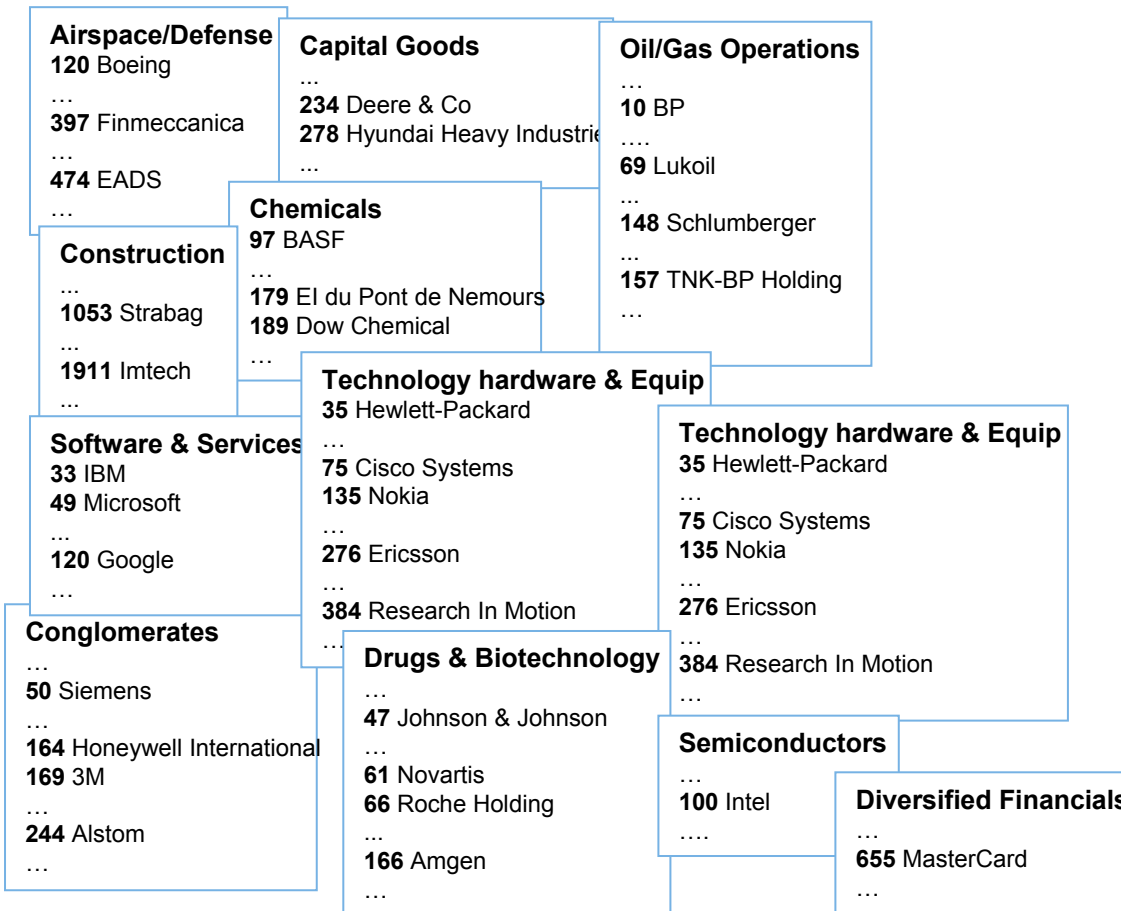
The process of identifying key corporate partners to be present at Skolkovo city is the process of matching those who (a) actually faces the need to for R&D tailored ecosystem to support its R&D and business development in Russia and thus shares enthusiasm and buys into Skolkovo initiative and (b) those who have respective valuable content to bring to ecosystem.



# Corporate Presence at Skolkovo. Negotiation Status.

Negotiations with up to 50 large corporations have already being initiated on their presence at Skolkovo city. First comers (Nokia, Lukoil, Cisco, Microsoft, Rosatom, Siemens, Intel, etc.) would seem to need about 20% of total about 1,5 thousand people slot allocated to be populated by corporate researches.

## Forbes Global 2000



## Estimated R&D division size at Skolkovo

Nokia	20-30
Lukoil	30
Cisco	(tbc)
Boeing	(tbc)
Microsoft	50
Rosatom	100-200
Siemens	50
TATA	(tbc)
Intel	50

By the summer 2011 major terms and forms of partnership will be agreed and documented with about 10-15 companies.





By the 11<sup>th</sup> of March 2011 28 start-up companies have been granted Skolkovo participant status and 10 companies have been approved for research grants for 107 mln. USD. In 2011 Skolkovo budget assumes 283 mln. USD of research grants to start-up companies.

