

Enabling Startups and Innovation in Russia and US



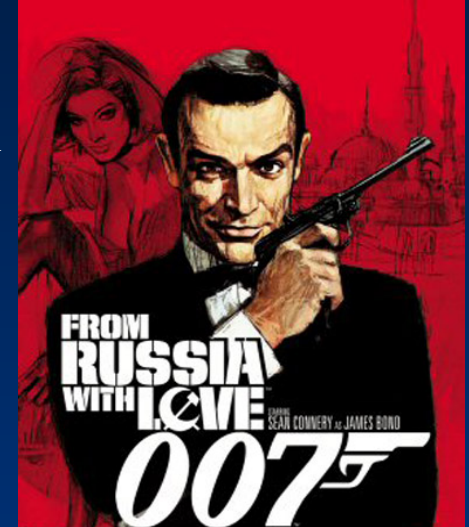
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Advantages and Disadvantages of Investing in Russian Startups

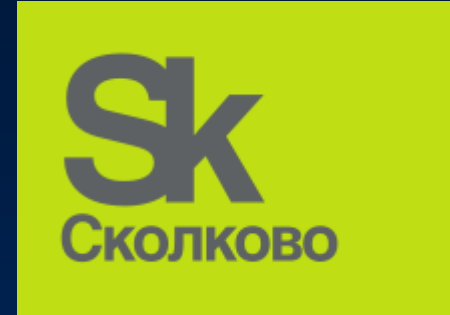
- Business Advantages:
 - Russia is the largest internet and mobile market in Europe, it has growing opportunities in other high-tech industries, from innovative software to nanotechnologies and clean tech to biomedicine;
 - Russia has a large and fast growing consumer market (GDP per capita has grown about 13% annually from 1999 through 2010)
 - High level of science and technology
 - Lower labor costs (except in Moscow)
 - More startups, stronger entrepreneurs, quickly developing ecosystem
- Disadvantages:
 - Corruption and bureaucracy
 - A few years behind western start-up scene in terms of finance and marketing



Practical Business Issues of Investing In Russian Startups

- Identifying Investment Targets
 - Databases, contests and media sources
 - Russia Beyond the Headlines (RBTH) has recently introduced their [Russian Startup Rating](#). The goal is to provide an objective assessment of the development level and dynamics of young technology companies established in Russia.
- Working with Incubators and Technoparks
 - **Skolkovo**, the state-sponsored tech hub nearing completion in southwest Moscow
 - **Ingria**, a prominent technopark and incubator in St. Petersburg
 - **Kazan's IT Park**, one of the largest technoparks in Europe

Incentives For Start-Ups and Innovation



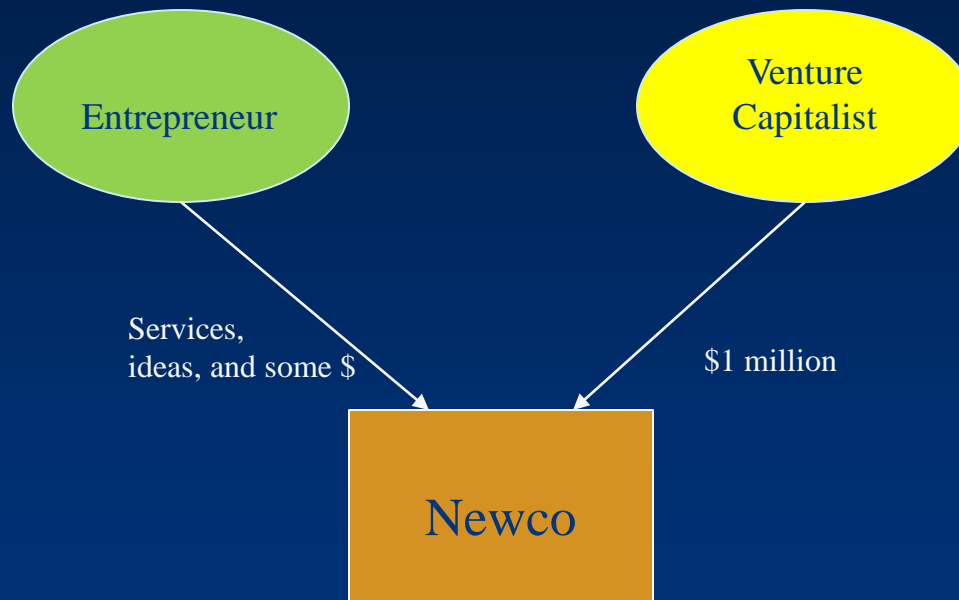
- Russian government's measures to support investments in start-ups
 - State controlled institutions investing in innovating companies (Russian Corporation of Nanotechnologies, Russian Venture Corporation, etc.)
 - Tax concessions for companies with high degree of intellectual capital (reduction of IT companies' social contributions from 30% to 14% until the end of year 2017; 0 profits tax rate for income received from disposal of shares in Russian hi-tech companies if certain conditions are met)
 - Russian Direct Investment Fund has \$10 billion that it is investing in PE in Russia and aims to attract international co-investors.
- Skolkovo Project
 - Exemption of Skolkovo residents from VAT, profits tax and property tax and a reduction of social contributions to 14% for 10 years
 - Companies who want to participate can be physically located elsewhere

Practical Business Issues of Investing In Russian Startups

- Co-Investing With Russian Funds
 - May be more advantageous to new foreign investors
 - Funds operate in accordance with international standards, care about their business reputation
 - For certain strategic sectors (e.g. oil, gas, defense), investing with a co-investor may be the simplest choice as strategic approvals may be required from the government which may not be forthcoming.
- Differences In Dealing with Russian vs. U.S. Entrepreneurs
 - Level of experience
 - Labor costs
 - English language proficiency

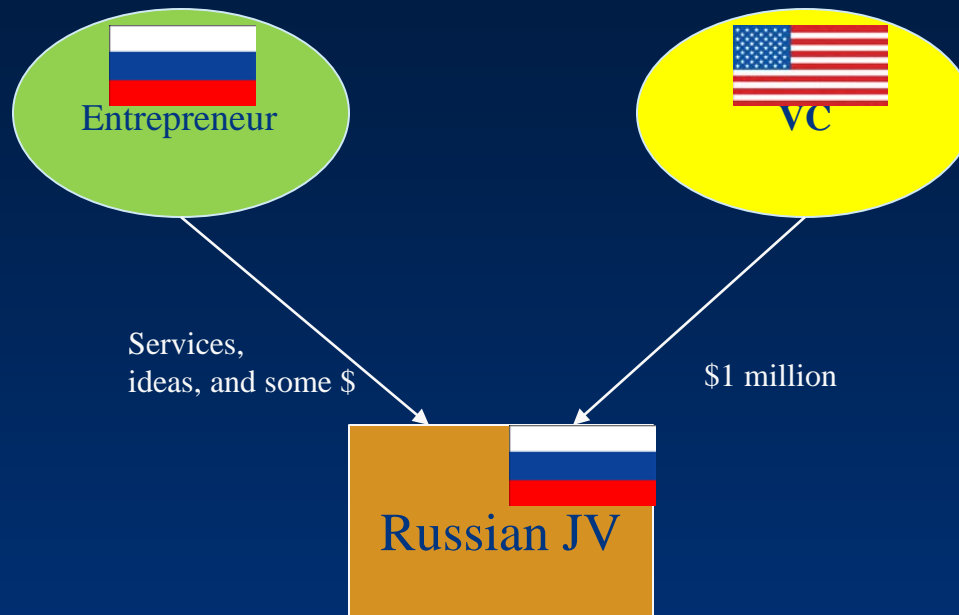


Structuring Start-Up Transaction-- General



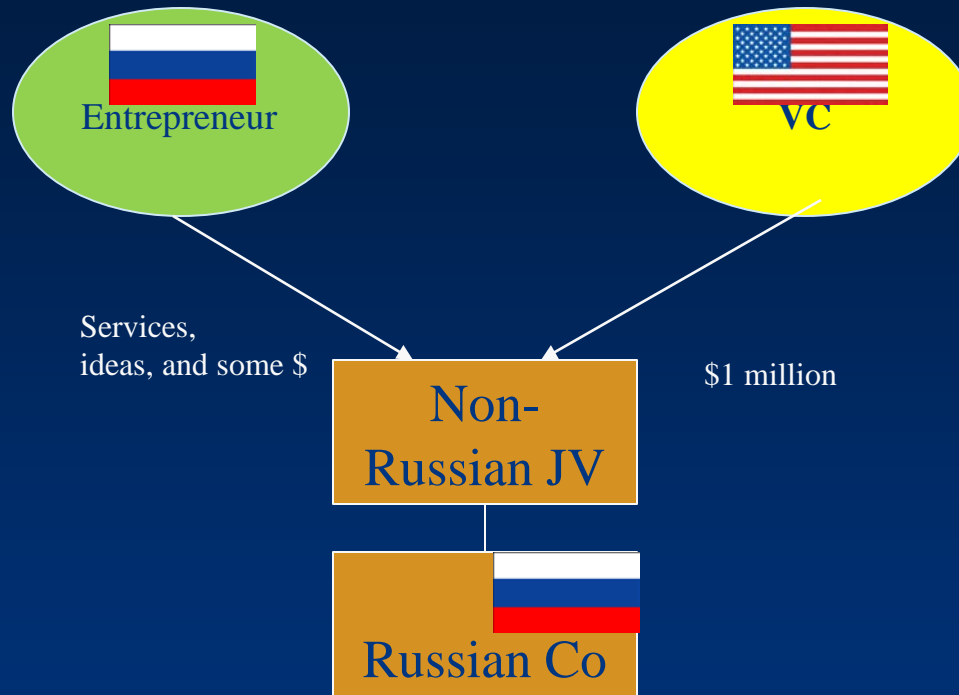
- Typical VC investment in the United States: various structures, VC may receive convertible preferred (or convertible debt) and common stock, E may receive common and options and profits interests (if Newco is an LLC)

Structuring Start-Up Investment in Russia with Non-Russian VC



- Using on-shore Russian JV
 - Russian side may be more familiar with the structure
 - May be cheaper than an offshore JV
 - Does not offer the level of commercial flexibility and certainty that a foreign VC expects
 - Russian courts do not have a good record of protecting shareholder rights generally and foreign investors rights in particular

Structuring Start-Up Investment in Russia with Non-Russian VC



- Non-Russian JV (Netherlands, BVI, Cyprus, etc.):

- Partners are governed by non-Russian law, legal disputes can be resolved by non-Russian court
- Structure can be complicated
- Management split between two legal entities
- For off-shore JVs, Russians are most familiar with a Cyprus holding company (due to reciprocal tax treaty with Russia), sometimes with a BVI Holdco on top

Types of Russian Companies

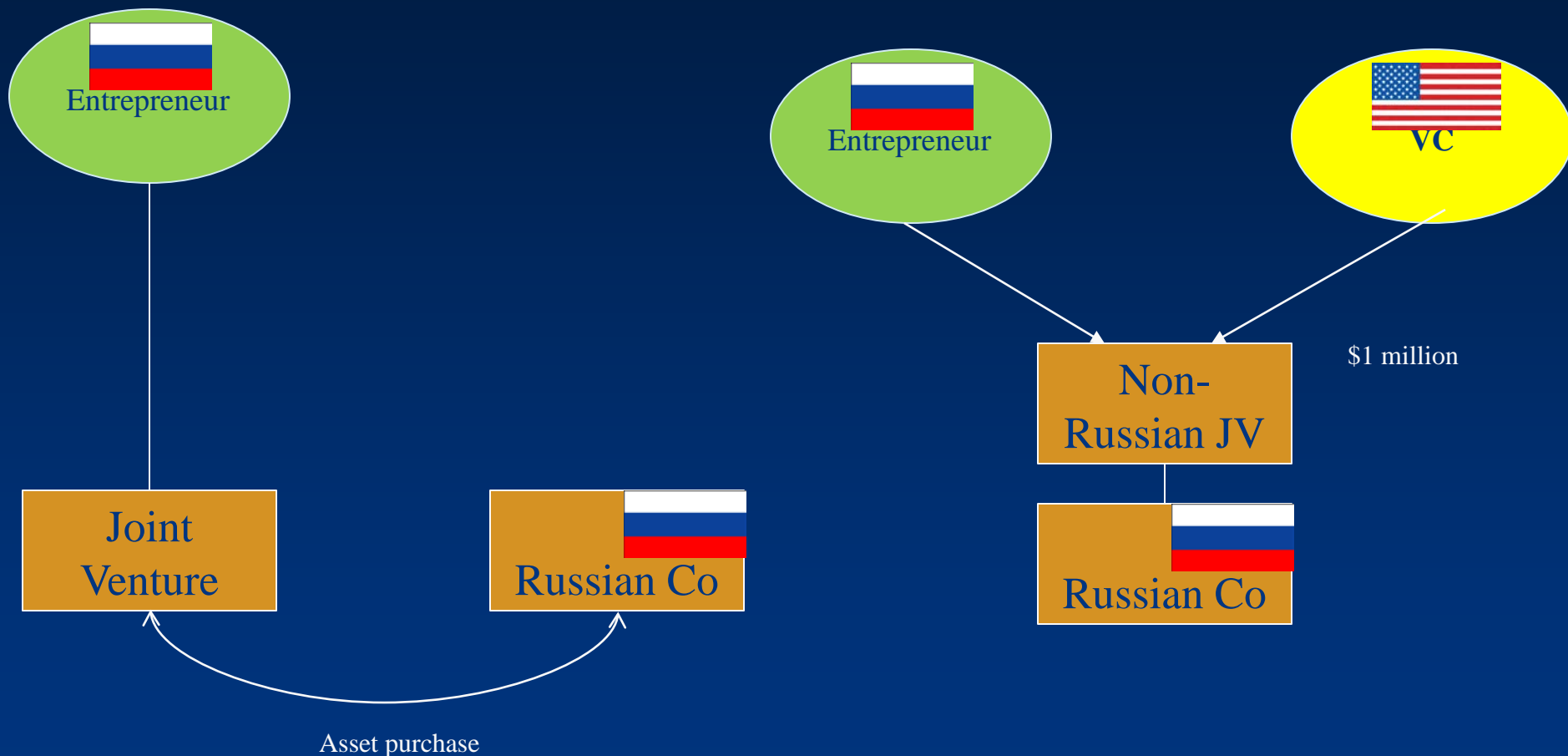
- **Russian Joint Stock Companies**

- open joint stock companies ("**OJSCs**" or "**OAO**" in Russian) and
- closed joint stock companies ("**CJSCs**" or "**ZAO**" in Russian)
 - The main distinctions between the two are:
 - CJSCs may not have more than 50 shareholders
 - CJSCs may not issue shares by open subscription i.e. a public offer of shares
 - acquisitions of more than 30% of voting shares in an OJSC trigger mandatory tender offer requirements and
 - shareholders in a CJSC have pre-emptive rights (i.e. rights of first refusal) to acquire shares sold by the other shareholders to third parties

- **Limited Liability Companies (“**LLC**” or “**OOO**” in Russian)**

- less regulated and rigid corporate vehicle. Unlike shares in Russian joint stock companies, issuance of equity or changes in capitalization of an LLC do not require registration with the FSFM
- The law provides LLC participants with more flexibility in managing their internal affairs and structuring corporate governance

Acquisition of a Russian Start-Up: Possible Structures



- Establishment of JV by Russian Entrepreneur, followed by acquisition of assets from Russian Co, followed by acquisition of shares in JV by VC
- Generally the transfer of assets in Russia can be very difficult, mired in red-tape and bureaucracy and time consuming

Stages of Proposed VC Investment

- Investor's initial due diligence
- Preliminary investment structuring (Russian vs. Non-Russian JV, new formation vs. acquisition of existing co)
- Term Sheet
- Legal diligence and contract drafting
- Definitive document negotiation (JV Agreement)
- Formation of JV Company
- Acquisition of Assets
- Acquisition of JV Interest by VC

Exit Opportunities From Russian Start-Ups

- Relatively young market, exit opportunities are not as efficient as in the U.S.
- Debt markets are closed (albeit there is a flurry of bond activity at the moment) as are the capital markets. Russian stocks haven't done that well.
- Selling the company to a strategic buyer or VC/PE Fund
- Exit opportunities to Western corporation who are looking to buy market share in Russia

Other Business and Legal Issues to Consider

- **Licensing Requirements**
 - Certain types of business activities can only be carried out in Russia with a special license issued by authorized licensing bodies
- **Land Ownership Issues**
- **Taxation**
- **Transfer Pricing**
- **Company and Labor Law**

Thank You!

Спасибо!

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