

THE CHINESE UNIVERSITY OF HONG KONG

Governance Framework for Subsidiaries and Spin-off Companies from The Chinese University of Hong Kong (Last updated and effective: 8th May 2018)

I. Preamble

- 1) Over the years, subsidiaries and spin-off companies from the University have been set up for various purposes. The benefits brought about by these companies and their activities include extending the knowledge and expertise of the University to the industry and community, and creating job opportunities.

Among other considerations, it is commonly accepted that a private limited company may be established and/or owned, whether wholly or otherwise, by a public-funded organization similar to the University:

- a) to hold properties, whether realties or equities, that may be acquired as a result of, or in relation to, the University's ancillary activities; for example, the CUHK Foundation Limited (CUHKF) which holds properties and shares that the University received from technology transfer and licensing activities;
 - b) for statutory requirements such as a separate entity required for the CUHK Shenzhen Research Institute (SZRI);
 - c) to encourage Faculty members and students to engage in entrepreneurial activities with their research results and innovations in the form of technology transfer;
 - d) to facilitate incubation of new companies set up by individual staff or students, often together with external partners, to commercialize their innovations or technology, where the University or the individuals may take shareholdings (usually a minority one) in those companies; examples are spin-off companies held by the INL, a subsidiary wholly owned by CUHKF and managed by the Centre for Innovation and Technology of the Faculty of Engineering;
 - e) for the transfer of knowledge to and delivery of services to the community in the form of a self-funded organization;
 - f) for the good practice of independent accounting and operations of separate entities, that no interference should be caused by these companies to the core activities of the University, and to protect the University from any liability in case arising from them;
- 2) The University Grants Committee (UGC) has a set of definitions of spin-off companies in the Common Data Collection Form (CDCF) for input by institutions on an annual basis:

Type A	Start-up company
Type B	Spin-off company
Type C	Technology-associated company
Type D	Incubating company

More detailed descriptions of these companies are contained in **Annex 1**.

- 3) These subsidiaries and spin-offs vary in business nature, purposes of establishment, and shareholding by CUHK. For instance, the subsidiaries are wholly-owned by the CUHKF, whilst the CUHK shareholding in spin-offs ranges from 49% to a very minority share.

II. Proposed Framework

- 4) To encourage innovations and services to the community, and to promote good practice, a framework and pertinent policies were formed for the Establishment, Governance and Development of subsidiaries and spin-offs.
- 5) It is recognized that different subsidiaries or spin-offs can be at different stages of their development or business life cycle. There needs a good environment and framework for new ones to establish, existing ones to develop, and the mature ones to be fully spun off from the University.
- 6) At the same time, the University also needs the framework to decide on strategies and options across the spectrum from increasing investment to initiating an exit from the company.
- 7) The University can consider keeping in its profile those companies:-
 - a) for social service with secure funding source, which is also a good window of Knowledge Transfer (KT) and a platform of further research, thus enhancing the reputation of the University and exemplifying its care for the community;
 - b) which serve as a business arm of the University and a bridge between the academia and industry, and are established with a specific mandate under a good monitoring system and in a good financial position.
- 8) The University should consider an exit, whether through winding up or disposal of shares, from companies:
 - a) which purpose for establishment has been fulfilled and/or completed;
 - b) which have been dormant for two or more years; or,
 - c) which have been identified as no longer viable to maintain.

III. Details of the Framework

The Framework should apply to all subsidiaries and spin-offs, whether new or existing ones.

Establishment

9) Whether to set up a new company

In deciding whether to establish a subsidiary or spin-off company, the University must consider, and the applicant must provide justifications, on whether there is a genuine need to do so, and whether other available platforms and channels (e.g. licensing) have been explored and found to be of a lesser advantage than the subsidiary/spin-off option.

In addition, the subsidiary/spin-off must be for one or more of the purposes as described in paragraphs (1)(a) to (e) above.

10) Who can apply for, or initiate, the establishment of a company (the Applicant)

- a) The University
- b) A CUHK Faculty/Department/Research Institute (non-Faculty based), as represented by the Faculty Dean/Department Chairman/Director of Research Institute (non-Faculty based)
- c) A CUHK full-time academic or research staff member
- d) For a team of Applicants, a Principal Applicant, who must be a CUHK full-time academic or research staff member, should be identified

11) How to apply for establishing one

The application must be endorsed by (a) the Chairman of Department/Director of School, and Dean of Faculty, or (b) Dean of Faculty only, for Faculties without the establishment of Departments, or (c) the Pro-Vice-Chancellor (Research) for non-Faculty based Research Institutes, before being first submitted to the Office of Research and Knowledge Transfer Services (ORKTS).

The application should include an Application Form and a full set of supporting documents, as listed in **Annex 2**.

12) Where should the new company be set up

In order to protect the University, incorporation of company is the more transparent the better. Generally, overseas company should not be established if it is wholly-owned by the University.

13) The Application

13.1 Information to be provided in the application should include:

- a) company name, objective of the company;
- b) a market survey and assessment;
- c) business plan, budget plan, marketing plan;
- d) Key Performance Indicators with timeframes;
- e) proposed composition of the Board of Directors, management team and structure;

- f) proposed shareholding, including that of the University;
- g) proposed income sharing among the University, Applicant, Faculty/Department, partners (if any);
- h) any overhead payments to the University;
- i) an undertaking of the Applicant on commitments to the proposed subsidiary or spin-off company;
- j) proposed review and exit plan; and
- k) information of the related intellectual property rights, e.g. patent, know-how etc.

13.2 Generally, the University should not accept equity (shares or stock options) in lieu of cash payment in a licensing deal. If the University is to accept shares, a Shareholder Agreement has to be drawn up covering items (e) to (k) of 13.1 above, if approved, and include without limitation:

- a) Duration (i.e. term of contract) and termination mechanism;
- b) Any use of the University's name or logo, or implying any association to the name of the University in the company name, must be subject to the University's prior written approval;
- c) CUHK's power to appoint Director(s);
- d) Directors appointed by the CUHKF should report to CUHK/CUHKF and disclose to CUHK/CUHKF any information relating to the company's affairs and shares and any matters which may affect the interests of CUHK/CUHKF;
- e) subsidiaries or spin-off companies should make available and promptly disclose all company's documents such as books, accounts, other financial records and management structure to the shareholders, CUHK or its authorized representatives for inspection;
- f) provision on increase of share capital and contribution of working capital;
- g) rules and procedures for appointment of key personnel;
- h) Directors should have a duty to establish rules on disclosure and ensure compliance of such rules in areas of operations where conflict of interests may arise such as procurement and personnel matters;
- i) appointment of auditors by CUHKF, particularly when CUHK is a minority shareholder;
- j) CUHK's veto power;
- k) CUHK's right to transfer shareholding at its sole discretion without restrictions;
- l) CUHK's tag-along right; and
- m) Directors should comply with all applicable laws and regulations of Hong Kong, including the Prevention of Bribery Ordinance (Chapter 201).

14) Approving Authorities

The application will be examined by the **Committee on University Subsidiaries and Spin-off Companies** (CUSSOC with details below), and requires the initial approval of this Committee, and then the final approval of the Administrative and Planning Committee (AAPC) of the University. Sufficient time should be allowed from submission to vetting and approval of applications, which will normally take at least 2 to 3 months.

Composition of CUSSOC

Chairman	Pro-Vice-Chancellor (Research)
<i>Ex officio</i> Members	Pro-Vice-Chancellor/Vice President (Administration)
	Chairman of the Patent Committee
	Chairman of the Committee on Knowledge Transfer
	Bursar or representative
	Secretary or representative
Members (for each term of two years, unless otherwise specified)	Community Member(s) nominated by the Vice-Chancellor
	An Academic Staff Member nominated by the Vice-Chancellor
	Director of the Centre for Innovation and Technology or representative
	Director of the Centre for Entrepreneurship or representative
	Dean or representative of the Faculty from which the application for the proposed company is initiated (if any, for the particular meeting only)
Secretary	Director or Director of KT, Office of Research and Knowledge Transfer Services

CUSSOC members shall declare any conflict of interest to the meeting as appropriate. Such members may be required to refrain from discussing about a specific issue or to abstain from voting on certain decisions in light of the declared conflicts.

Terms of Reference

- a) To devise strategies to promote Knowledge Transfer through subsidiaries and spin-off companies of the University.
- b) To examine applications for establishment of new subsidiaries and spin-off companies, and provide initial approval, if appropriate, for the final approval of AAPC.
- c) To examine and approve annual reports of companies; and to recommend to AAPC, if appropriate, further investment, or disposal of shares or assets, or withdrawal from or winding up of companies.
- d) To monitor the development of companies and appoint a task force or sub-committee to assist in the discharge of its duties as and when required.
- e) To maintain a central record of CUHK subsidiaries and spin-off companies.

15) Board of Directors

Requirements for the composition of the new company's Board of Directors are as follows:

- a) For a company to be wholly owned by CUHKF, or where CUHKF has a shareholding of more than 50% of the issued shares -

The number of Directors appointed by the University must account for a majority on the Board, and should include but not limited to:

- Pro-Vice-Chancellor (Research) or representative [Chairman of the Board]
 - Bursar or representative
 - The Applicant
 - The Dean of the Faculty, or the Chairman of the Department, or the Director of the non-Faculty based Research Institute, to which the Applicant belongs
- b) For a company where CUHKF has a shareholding of less than 50% of the issued shares, the composition of the Board of Directors is to be negotiated between CUHK and the Applicant, and be initially approved by CUSSOC for the final approval of AAPC.

16) University Input and Shareholding

The University's shareholding in a company will depend on the nature of the case which the company relates to. Investment in monetary terms should not be considered. Rather, investments in kind may be considered, for examples, through technology transfer, provision of IP or facilities (whether premises, equipment or other resources, e.g. human or management).

Generally speaking, University shareholding can be categorised into two types.

a) IP-related Companies

Where IP is involved or arises from activities of the company, CUSSOC may make reference to the guidelines on the division of income under the University “Policy on Research, Intellectual Property and Knowledge Transfer” to propose the size of University shareholding.

According to the prevailing Guidelines, the division of income should be based on the established ratios,¹ which will be determined by the inventor’s contribution towards the filing of patents or registration of any IP (i.e. contribution of 0%, 50% or 100% for 25%, 50% or 75% respectively of the income to the inventor). The non-inventor’s shares of the company will then be divided between the University Central Fund and the Faculty concerned at the established ratio of 60:40. In respect of the Faculty’s 40%, the Faculty Dean will have the discretion to make appropriate distribution to the department/unit.

Proposed Division of Shareholding		
<i>Inventor Contributions towards patent filing / IP registration costs</i>	<i>Inventor Shareholding</i>	<i>University Shareholding²</i>
Nil	25%	75%
50%	49%	51%
100%	75%	25%

b) Non-IP related Companies

Where IP is not involved or does not arise from activities of the company, University shareholding should be proposed by CUSSOC taking into consideration factors such

¹ Paragraphs 9.4 and 9.5 of CUHK Policy on Research, Intellectual Property and Knowledge Transfer

² To be divided between the University Central Fund and the Faculty in the ratio of 60:40

as resources that have been or may be committed by the University, including facilities, space, manpower and equipment.

Governance and Management Strategy

17) Commitments of Directors appointed by CUHKF

Directors who accept an appointment by CUHKF to the company Board should understand that being a Director requires substantial commitment in both efforts and time, and is subject to regulatory oversights. Such Directors should be familiar with duties of company directors according to the Companies Ordinance (Cap. 622). Directors should therefore attend director training programme and read relevant guidelines.

Directors shall undertake in writing to the University to:

- a) disclose any conflict of interests;
- b) exercise due diligence and care;
- c) keep in confidence any information available during the term of office;
- d) safeguard the University's interests, particularly in case of any conflict;
- e) not to use the University's name or logo, or publish or use any advertising or publicity material from which an association with the University can reasonably be inferred or implied without the prior written consent of the University; and
- f) indemnify the University for any wilful or reckless act of himself/herself which cause detriment or damage to the University.

18) Commitments of Applicants

In addition to points (a) to (f) in paragraph 17 above, the Applicant should undertake to the University to:

- a) remain to be in service to the company for at least three calendar years from its formation, unless so required by the University to the contrary. If the Applicant left the University, it would be up to the University to nominate another person to take over the Applicant's place;
- b) provide in a timely manner the required reports, including but not limited to performance report, financial report(s), forecast report, business plan, exit plan and those listed in **Annex 3**, to the University via ORKTS to ensure legal compliance; and for this purpose enter into a "Reporting Agreement" with the University at the formation of the company;
- c) attend review meetings in the annual review exercise of CUSSOC, answer questions at review and anytime from CUSSOC, the Bursary or the ORKTS;
- d) report to CUSSOC through ORKTS in writing within 7 days upon notice from the company board meeting or having knowledge of any change or factor which may affect the University shareholding, for CUSSOC's consideration of corresponding strategies in the face of such change; and

- e) provide information and other reports as and when required by UGC or other stakeholders, and for publicity when needed.

19) Obligations of participating CUHK staff

As long as a University employee participates in the running of a company in whatever capacity or level, irrespective of whether monetary or other in-kind return is involved, such participation must be subject to the prevailing University personnel policies, and the Policy on Research, Intellectual Property and Knowledge Transfer. The participant must also provide a written undertaking to the University as detailed in points (a) to (f) in paragraph 17 above, before an approval for the participation can be considered.

University employees should refrain from engaging in commercial activities or forming companies which may cause damages to the University (e.g. to its reputation).

The Applicant must report to the Pro-Vice-Chancellor (Research) if he/she will no longer be in full-time employment with CUHK. This should be done within one week after the arrangement has been confirmed with the Personnel Office. Resignation from directorship in the company must be submitted to the Pro-Vice-Chancellor (Research) at least three months from the effective date.

20) Company Secretary

A professional agent/firm must be engaged as the Company Secretary for new companies. Existing Companies should also consider such engagement.

21) Requirements for Companies

The requirements for reporting and for obligations of participating CUHK staff will apply to all new and existing companies. Non-compliance will be reported to the Dean of Faculty and Chairman of Department to which the Principal Applicant (or Principal Investigator for existing companies) belongs.

Companies wholly owned by CUHKF or where CUHKF has a shareholding of more than 50% of the issued shares, either directly or indirectly, have to draw up a code of conduct and procurement guidelines for company's integrity management.

22) Incentives for Staff

Upon the encouragement of UGC for institutions to provide practical incentives for academic staff to actively participate in the commercialization of research output, the University can consider approving half-time employment or no-pay leave for 6 months for staff to work full-time for subsidiaries and spin-off companies, so as to provide enabling conditions for the companies especially at the formation stage.

23) Review and Exit

On the basis of periodic reports of the companies and their performance and the wider environment, the CUSSOC will review subsidiaries and spin-off companies after the

end of each financial year (generally from 1 July to 30 June of following year), and if deemed appropriate, on a more frequent basis.

Companies should provide performance report, financial report(s), forecast report, business plan, exit plan for CUSSOC's consideration.

CUSSOC can make winding up decisions for the University as appropriate and no further approval is required. For companies where CUHKF was a shareholder, the CUSSOC Chairperson, being a Director of CUHKF with delegated authority, would report the decision of CUSSOC to CUHKF.

All new and existing companies should have an exit strategy (through disposal or winding up) for the University to withdraw, if deemed necessary, from the company overtime as it matures.

ORKTS will assist CUSSOC to organize subsidiaries and spin-off companies into four categories for devising the exit strategy as appropriate:

Category A: Longer Term Companies

Companies in this category are those:-

- a) for a genuine requirement or business need of the University to hold, e.g. CUHKF [ref. paragraph (1)(a)]; or
- b) strategically important for the University to retain its participation in them; or
- c) for the University to maintain a profile of high social impact on the wider scope of KT as highly regarded by the UGC [ref. paragraph (7)(a)].

In addition, these companies should be generally in a sound position financially and operation-wise, and are of low risk to the reputation of the University.

Strategy: Unless problems are identified in the periodic reviews or the company has developed into Category B or C below, these companies will be kept by the University on a continuous basis or over a longer term.

Category B: Start-ups or Incubatees with Milestones for Spinning off

- a) Typical of this kind are start-up companies initially set up by faculty staff or students to commercialize their innovations or technology.
- b) It has to be noted that NOT ALL start-ups or incubatees have to be held by or need to have the participation of the University. The companies in this category refer to those which are identified by CUSSOC to have the strategic need or benefit for the University to hold, in part or in whole. A typical example will be one having good prospects of being acquired by investors with good income and benefits to the University.

Strategy: Each company, according to the market situation and business context it is in, should have milestones set at its beginning, and adjusted if necessary as a result of each review of it, for the period which the University should hold or participate in it, or for the stage at which the University should withdraw from it.

Category C: Up for Spinning off or Withdrawal

These companies are those already [ref. paragraph 8 (a)-(c)]:-

- a) mature for sale or being spun off; or
- b) having its purpose of establishment fulfilled and/or completed; or
- c) its purpose of establishment is no longer relevant or clearly cannot be fulfilled;
or
- d) inactive or dormant for two years or more, or
- e) not complying with the legal, regulatory or reporting requirements; or
- f) of poor performance, or high financial, operational or reputational risks to the University.

Strategy: Action should be taken for the University to withdraw from them as soon as possible [ref. paragraph 8].

Category D: Exempt Category

These companies are those:-

- a) which the University does not hold any shares or has any control. These companies are for internal record only therefore should not be reported under UGC's CDCF or in the annual KT report; or
- b) which is under another governing structure of the University.

The categorization of companies may change upon each review of them as they evolve or develop.

If a CUHK staff member wishes to maintain his/her participation in a company after the University has withdrawn from it, the participation will be regarded as Outside Practice and is subject to relevant personnel policies.

24) IP

Once a company is formed, legally it is independent from the University; and any use of University IP by it, or transfer of IP to it, should be subject to prevailing University policies.

25) Cessation of Directorship

Directors appointed by CUHKF must agree in writing that upon cessation of their directorship, they shall not be entitled to any compensation, including compensation for loss of office. Directors shall be obliged to keep in confidence any information available to them during the term of their office even after they have ceased to be a director.

26) Name and Logo of CUHK

Any use of the University's name or logo, or implying any association to the name of the University in the company name, must be subject to the University's prior written approval. The requirement is to be laid down in the Shareholder Agreement, Reporting Agreement, and Undertakings by Directors and the Applicant, as described in paragraph 17.

27) Role of ORKTS

The University is committed to ensuring high standards of corporate governance and providing a well defined organization and management structure in relation to subsidiaries and spins-off. CUSSOC is vested with responsibilities in accordance with the Terms of Reference in paragraph 14 and is supported by ORKTS. The major roles and functions of ORKTS are to:

- a) assist CUSSOC in formulating policies and guidelines in relation to subsidiaries and spin-off companies;
- b) advise faculty members on the policies and guidelines;
- c) oversee subsidiaries and spin-off companies' compliance with CUSSOC's policies and requirements including without limitation the required half-yearly/annual management reports;
- d) review and make recommendations to CUSSOC as to the management and progress of companies;
- e) invite expert advice or assistance within or outside of CUHK as and when necessary; and
- f) provide committee service to CUSSOC.

It will not be the role of ORKTS in the formation and dissolution of companies if any relevant personnel is/are still in CUHK employ. However, if all relevant personnel left their employs, ORKTS will coordinate and work with the Department or Unit to facilitate the completion of the dissolution/winding up procedures and share transfer process. During such process, ORKTS can also engage professional/consultant when necessary, e.g. for evaluation of share price for transfer, company search or legal advice. CUSSOC can utilize the money allocated by CUHKF to ORKTS for such purpose.

IV. Implementation

28) This paper seeks to establish the framework for more comprehensive management of University subsidiaries and spin-off companies. Details for the implementation are to be worked out by the Pro-Vice-Chancellor (Research) and ORKTS.

Professor Fanny M C Cheung Pro-Vice-Chancellor (Research)
8th May 2018

G7 Companies with Knowledge Transfer and Other Related Companies [formerly F17]

The companies are classified into 4 types as follows:

A1-A3: Start-up company

- A start-up company is one that has been *established by staff, graduates or students* and which is at present still *operationally dependent* of the institutions (e.g. the institution has a participating role in the management of the company; the institution serves on the Board of Directors of the company; the institution has a decision-making role of the company).

A1: Start-up company established by staff

A2: Start-up company established by graduate

A3: Start-up company established by student

B1-B3: Spin-off company

- A spin-off company is one that has been *established by staff, graduates or students* and is now *operationally independent of the institution*.

B1: Spin-off company established by staff

B2: Spin-off company established by graduate

B3: Spin-off company established by student

C: Technology-associated company

- A technology-associated company is one *other than a start-up or spin-off company* in which the *institution holds an equity* by virtue of technology transfer (e.g. company providing a service that was originally offered through the institution’s department or unit).

D: Incubating company

- An incubating company is one *other than a start-up or spin-off company* in which *institution does not hold an equity* but which is *using the institution’s incubation facilities* (through, say, licensing arrangement) for their research.

A table listing the different scenarios (though some scenarios may rarely exist in reality) for classifying the various types of companies according to the above criteria is given below for reference:

Case	Establishment (founding shareholders by institution’s members)	Institution holds equity	Operational dependent	Use incubating facilities of the Institution	Classification
1	Y	Y	Y	Y	Start-up
2	Y	Y	Y	N	Start-up
3	Y	N	Y	Y	Start-up
4	Y	N	Y	N	Start-up
5	Y	Y	N	Y	Spin-off
6	Y	Y	N	N	Spin-off
7	Y	N	N	N	Spin-off
8	N	Y	Y	Y	Technology-associated
9	N	Y	N	Y	Technology-associated
10	N	Y	Y	N	Technology-associated
11	N	Y	N	N	Technology-associated
12	Y	N	N	Y	Incubating
13	N	N	Y	Y	Incubating
14	N	N	N	Y	Incubating
15	N	N	Y	N	Excluded from data collection
16	N	N	N	N	Excluded from data collection

Application for the Establishment of a Subsidiary or Spin-off Company

Documents required

1. Application Form (designed by ORKTS)
2. Supporting documents
 - (a) Description of technologies / services / goods
 - (b) Patent / Patent Application documents, if any
 - (c) Market survey and assessment;
 - (d) Marketing plan;
 - (e) Business plan;
 - (f) Budget plan;
 - (g) Key Performance Indicators with timeframes;
 - (h) Proposed composition of the Board of Directors, management team and structure;
 - (i) Proposed shareholding, including that of the University;
 - (j) Proposed income sharing among the University, Applicant, Faculty/Department, partners (if any);
 - (k) any overhead payments to the University;
 - (l) an undertaking of the Applicant on commitments to the proposed subsidiary or spin-off company;
 - (m) proposed review and exit plan;
 - (n) information of the related intellectual property rights, e.g. patent, know-how etc.

Reports on the Company to be provided via the Applicant

- 1. Establishment report**
to be submitted immediately after the formation of the company.
- 2. Half-yearly/ Annual Management Report with:**
 - (a) particulars of business activities within the reporting period;
 - (b) particulars of cash flow;
 - (c) particulars of acquisitions in excess of HK\$10,000 per item and HK\$50,000 in accumulated cost;
 - (d) number of products produced and sold, and to account for the difference, if any;
 - (e) particulars of any change in management structure;
 - (f) fulfilment against Key Performance Indicators.