

**SHENZHEN PRESENTATION**

**STRUCTURING THE SPIN-OUT OF IP TO CREATE A NEW VENTURE**

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**BY:**

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**I. Reasons for Spinning Out**

- A. Create ability of Chinese company to access capital in United States
- B. Free the venture from Chinese parent's resource allocation and planning decisions and other constraints, which may not be consistent with health and growth of venture
- C. Different risk profile –investment in new market compared with familiar, existing business
- D. Liberate parent from funding responsibilities
- E. Encourage entrepreneurial spirit; increase focus
- F. Recruit talent that might not be attracted to internal division or venture
- G. Employee ownership

**II. Technology Transfer Structure**

- A. Assignment vs. license

- B. License
  - 1. Exclusive vs. nonexclusive
  - 2. Field of use
  - 3. Retention of rights by parent; License back to parent for certain uses
  - 4. Infringement by third parties; Infringement on the rights of third parties
  - 5. Improvements
- C. Ownership issues if continued joint development

### **III. Economic Terms**

- A. Contributions by parent
  - 1. Intellectual Property
  - 2. Valuation of the Intellectual Property
    - a. Function of R&D expense attributable to the technology
    - b. Function of valuation of technology if sold currently to a third party
    - c. Negotiation with outside investors
    - d. Equity vs. Royalties. Create a “win-win” structure. Consider use of convertible preferred stock with liquidation preference equal to agreed upon current value to preserve cash in the venture
    - e. Use of milestones to adjust consideration to parent (conversion ratio adjustment or issuance of Warrant) subsequently if value is ambiguous
  - 3. Other assets
    - a. furniture, fixtures or equipment
    - b. intangible/contracts
    - c. infrastructure services (HR, accounting, etc.)
    - d. temporary facility sharing

- 4. Financial support – seed financing; follow on funding; commitment to participation in later outside financing round(s)
- B. Contribution by new investors (generally cash for preferred stock)
- C. Equity participation by management -- Individuals treated as founders?
- D. Continuing commercial relationship between parent and new venture
  - 1. Vendor/Customer
  - 2. Support services
  - 3. Joint R&D
- E. Competition between parent and new venture
  - 1. For customers
  - 2. For employees

#### **IV. Governance**

- A. Constitution of Board of Directors
  - 1. Parent represented
    - a. Director
    - b. Observer
  - 2. Management represented
  - 3. Outside investors represented
  - 4. Procedure for selecting independent directors
- B. Protective Provisions (voting, special consent rights of parent, etc.)
  - 1. Parent
  - 2. Outside investors

#### **V. Conflicts of Interest**

- A. Parties:
  - 1. The parent

2. The new venture
  3. Outside investors
  4. Management/founders
- B. Parent on both sides of transaction
1. Watching out for interests of new venture
  2. Watching out for interests of management
  3. Are interests naturally aligned?
- C. Impact on employees of new venture
1. Can they effectively negotiate?
  2. Potential negative impact on future success of venture?
  3. Consider designating roles (i.e., founder/management to look out primarily for interests of Newco, even though still employed by parent, and parent executive to look out primarily for interests of parent)
- D. Preserving role for Parent
1. Retain Chinese/Asian Rights
  2. Manufacture Product in China

## **VI. Human Issues**

- A. Who goes with Newco? Who stays with parent?
- B. Can parent tolerate loss of talent?

Alternative arrangements (allowing parent to keep people)

1. Compensation/incentive issues
2. Accentuated conflicts of interest

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Steven M. Cohen is a partner in the Emerging Business and Technology Practice. Mr. Cohen's practice focuses on advising emerging growth companies throughout the mid-Atlantic. He is experienced in representing companies and investors in venture capital financings, representing issuers in IPOs and secondary public offerings, acquisitions, divestitures and mergers, joint ventures and strategic partnerships, and providing general corporate and securities advice to publicly held corporations and limited partnerships.

Mr. Cohen has significant experience assisting biotechnology, information technology, consumer products and other companies in planning for and implementing growth strategies, including making the introductions required to make deals happen.

Mr. Cohen is a member of the Board of Directors of the New Jersey Technology Council and is also active in the New Jersey Entrepreneurs Network and the Entrepreneurs Forum of Greater Philadelphia. Mr. Cohen is a frequent speaker on obtaining financing for emerging growth companies and planning profitable exit strategies.

**Honors & Affiliations**

Listed, *Chambers USA: America's Leading Lawyers for Business* (2003-2006)

Listed, *The Best Lawyers in America* (2006)

Top New Jersey Deal Maker, *NJBIZ* (2002)

Top 40 Under 40, *NJBIZ* and *NJ Lawyer* (2002)

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Irene Chiu is an associate in the Business Transactions Practice. Ms. Chiu's practice focuses on representing public and private companies in mergers and acquisitions; advising emerging growth companies and investors in venture capital financing; forming joint ventures, partnerships, corporations, and other forms of entity; and counseling clients on general business law and corporate & securities law.

Ms. Chiu also represents and advises information technology and life sciences clients regarding collaboration, strategic alliances, licensing, intellectual property rights, outsourcing and commercialization of technology assets; counsels manufacturing companies regarding distribution and supply agreements; and negotiates clinical trial agreements for domestic and international pharmaceutical companies.

Ms. Chiu has experience with clients doing business in China and Hong Kong, including joint ventures, wholly foreign-owned entities, manufacturing, licensing, distribution and supply arrangements. Ms. Chiu is fluent in Chinese and possesses a conversational level of Japanese.

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Member, American Bar Association

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