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Gawlik, Remigiusz and Teczke, Janusz

Cracow University of Economics

2003

Online at <https://mpra.ub.uni-muenchen.de/45224/>
MPRA Paper No. 45224, posted 11 Apr 2013 12:09 UTC

SPIN – OFF ENTERPRISES AS A FINANCING SOLUTION FOR THE INNOVATIVE CLIENTS OF SCIENCE AND TECHNOLOGY PARKS

J. TECZKE, R. GAWLIK

Cracow University of Economics, ul. Rakowicka 27, 31-510 Kraków, Poland

elteczke@cyf-kr.edu.pl; remigiusz.gawlik@neo.pl

Abstract: In this paper we try to present the role of one of the Venture Capital financing solutions - the Spin – off organizations, which are a very interesting way of acquiring the financial means for the new established innovative companies – clients of the Science and Technology Parks.

Keywords: Spin – off, Science and Technology Park, Innovation, Alternative Financing, Venture Capital

1. Introduction

The division between the capital owners and those who have got interesting ideas, but do not possess enough means to put their projects into business practise has existed since the very beginning of the capitalism. Today, in the global economical environment, this partition can be observed even more then before. The cause of such a sharpening of the mentioned division line is the actual business environment, with aggressive marketing and very high level of market saturation in almost every area of life. The important change occurred in the thinking of the businessmen – they are not selling products anymore, but whole lifestyles, ideas or fashions. Because of that, to start a business today, the fact of having money and organisational abilities is not sufficient enough. What really sells, are innovative ideas.

Meanwhile we can easily imagine a situation, where a young constructor, who has an interesting idea of an innovative solution and a very strong belief, that with some financial and organisational help he could first develop and then commercialise his product, has no financial means at all. As he is young and not employed on a basis of a full - time work contract, he is not a credible client for banks when applying for a credit. Eventually, even if he manages to get one, its amount would probably be much too low and at the end he will not have enough organisational experience to lead his commercialisation project to a successful end. It is also probable, that he would better like to spend his time on improving his project quality, instead of doing all the management work.

For such people, a good solution can be cooperation with a Science and Technology Park grounded in their city or region. Such places are platforms of cooperation between the local high schools, science and advanced technology promotion centres and the potential investors. Each of these groups has its own advantages against the others. The high schools provide a sufficient number of

well educated and highly specialised personnel, as well as management and organisation specialists, the science and advanced technology promotion centres bring the technological and scientific know – how. Their role is also assuring the constant technological or scientific development of the young company by providing the latest news from the concerned domain. The investors bring money into the projects they evaluate as those who could bring important benefits in the middle – or long - term future (usually 5 to 10 years, with a high risk rate, but the more risk, the more revenue on capital possible). The role of the Science and Technology Park itself is to provide necessary buildings (office rooms, production halls), infrastructure and office help. As a good business comes off from a mix of all of the above, establishing a company in a science and Technology Park gives the young enterprise the key prosperity factors.

2. What is a Spin – off enterprise?

The Spin – off is being created when a need of technological know – how transfer occurs. Usually, the transfer starts in a research and development unit and its direction is a recently established unit, which aim is finding a solution of use of the acquired technology in practise and its commercialisation. We have to underline here, that this kind of knowledge transfer can be used both for new and already existing products.

In practise, a Spin – off creation consists in separating the assets of an existing enterprise in the form of a venture capital fund, notwithstanding any change of property rights – the lately created unit fully comes under the organisational chart of its mother company. Its role is to develop the conceptions and ideas coming from its mother enterprise, which are seen by the mother organisation as worth further improvement, but cannot be developed due to diverse reasons.

The management board of the young Spin – off enterprise consists of the managers delegated from the main enterprise – they leave their former employer and sign contracts with the Spin – off. It hardly ever occurs that any external managing board is hired. Due to such connotations of the management, every strategic decision is being made only after consultation with the mother company.

The main advantage of a Spin – off creation for the mother company is the fact of having an own research and development organisation. Partly independent on one hand, but on the other - bringing innovative solutions for the mother company and taking all the risk related to the development and commercialisation of the new technologies, which is much higher than in classical, stable business branches. Other advantage is a small, very flexible structure, fast reacting for the market needs and changes. The Spin – off permits the mother company to focus on its main areas of activity and creates better conditions for scientific and technological advance. At the same time, any

over - investment or project failure does not affect the mother company, but the Spin – off only.

Obviously, there are some disadvantages, too. One of them is the high risk of conflict of interests between the Spin – off and the mother company. Many of such conflicts result in an abrupt bonds breaking between both institutions, which is not profitable for any of them. However, in almost every Spin – off a moment arrives, when breaking the bonds with the mother company seems very tempting for its further development and commercialisation of the new technology. The problem is that the main enterprise hardly ever can be satisfied with cost repayment only. This is the moment, when in most cases negotiations start.

Other disadvantage of a Spin – off creation is the high organisational and juridical separation cost that has to be paid by the mother company and the high risk of losing the invested financial means.

The financial market knows several types of Spin – off enterprises. All of these can be mainly divided into two groups: the *real Spin – off* (new applications of already existing products) and *abstract Spin – off* (only transfer of technological knowledge)¹.

If we look on the organizational side of a Spin – off, we can name the *Spin – off without enterprise creation* and the *Spin – off with enterprise creation*. In the last case, the role of the enterprise would be not only the implementation of the developed innovative technology, but also its use in production. This is the most common form of a Spin – off and further differentiation can be made: the *original* and *derivative Spin – off*. The *original Spin – off* did not have any organizational structure before the start of the new activity, and the *derivative Spin – off* used to have one. As one can easily understand, the *original Spin – off* has to be created from the beginning to the end, and the *derivative Spin – off* can be based on an already existing organizational structure.

A very important point in the original Spin – off creation is the position of the mother company against the new economic subject. If the Spin – off is being created in cooperation and after a positive decision of the mother enterprise, it can count on further financial, essential and organisational help. Meanwhile, sometimes the mother company does not see enough profits in creating an independent research and development unit. If the managers are strongly convinced, that the new enterprise can still be successful, they create a *Split – off*, which acts on the same rules, as the *original Spin – off*, but cannot count on any kind of help from the mother company. At the same time, it is independent and very fast becomes subject of usual rough market games – there is no protection from the mother company's side.

The forms of *derivative Spin – offs*, that can be observed in business practise are *spin – outs* (a new organisational unit is being created as a part of an existing enterprise) or *partial* and *full buy – outs*. The idea of a *buy out* is the

¹ N.Szyperski, H.Klandt, *Wissenschaftlich-technische Mitarbeiter von Forschungs- und Entwicklungseinrichtungen als potentielle Spin – off – Gründer*, Opladen 1981, s.19

sale of an up – to – now dependent organisational unit to an external business unit. The difference between *partial* and *full buy – outs* can be found in the level of shares acquired by the buyer – full block of shares (*full buy – out*) or a partial ownership share (*partial buy – out*).

It is the role of the mother company to decide the method, with use of which the Venture Capital will be brought to the established Spin – off. Many enterprises do not have interest in inviting the external investors. In this case, the company creates a Venture Capital fund itself, with the help of which the new innovative unit will be financed. Meanwhile, if the mother company allows the participation of other Venture Capital investors, both sides can gain important profits from the Spin – off activity. The external investors will have easy and cheap access to the experience of the stable, well market - implanted mother company. If the Spin – off becomes successful, they can also easily sell their shares to the mother company. On the other hand, both partners can gain profits by creating strong and background diverse research groups, grouping their own researchers in teams and gaining so the synergy effect.

3. Spin – off as a good financing proposition for an innovative enterprise – client of a Science and Technology Park

Like in every business, very fast the problem of financing the promising concept results. Here comes the Spin – off solution. In the following lines we will try to describe why it can be useful for the innovative clients of Science and Technology Parks.

First important feature is, that a Spin – off is always linked with innovation. The finance market offers very few financing instruments for the new, innovative technologies – most of classic financial instruments do not accept such a high level of risk, which always accompanies new technologies. Even Venture Capital funds that are mainly financing the innovative solutions do not assure such a strong linking with the constant development of the discovered innovation, as a Spin - off does.

Secondly, the Spin – off brings the organisational experience of the former mother company managers, which is very important when starting a new enterprise. It happens very often, that a young scientist, who has got interesting ideas does not want, or even cannot - because of lack of experience - devote enough of his time to management questions. The assistance of professional managers can be useful here.

The third feature that makes a Spin – off an interesting tool for financing the clients of science and technology parks is the direction of its further development – the company has to commercialise and sell or further use its new technology. And this follows exactly the main aim of every enterprise that was grounded in a Science and Technology Park.

4. Conclusion and proposal of a new solution

In this paper we tried to bring closer to the reader the definition of a Spin - off enterprise, the types of Spin – offs and its usefulness for a lately established innovative enterprise – the client of a Science and Technology Park.

Being one of the Venture Capital investment instruments, the Spin – off offers its beneficiaries interesting perspectives on further development of their projects and their successful commercialisation. It leaves also a possibility for the manager of buying or selling the enterprise when it becomes profitable.

Many of the existing Science and Technology Parks recommend to their customers this kind of business activity, which is – in our opinion – a very good start point for becoming successful on the difficult and risky market of today, where in fact only products with high level of innovation can offer very high revenue on capital.

To end up we would like to signal a possibility of creation of a new solution in the Spin – off area. An unusual, but very promising Spin – off grounding could be achieved by creating a Spin – off centre from a University or other higher education institution. The University's employers would be delegated for a two years period to work in the lately created Spin – off. During this time, as they would create the essential research and development background of the young company, they would not have to fulfil their scientific and didactic duties against their mother institution – the University. Once their contract with the Spin – off terminated, they would be back in their usual work at the high school.

Such a solution offers even stronger linking between the innovative side of the young Spin – off and its development potential. The reason is a perfect mix of scientific and management specialists, very needed for the prosperity of a young company.

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