Innovation and Technology Venture Fund

Frequently Asked Questions

Background

1. What is the Innovation and Technology Venture Fund?

The Government has set up a HK$2 billion Innovation and Technology Venture Fund (ITVF). The main purpose of the ITVF is to attract more private funding to the innovation and technology (I&T) ecosystem in Hong Kong. The ITVF, through a special-purpose vehicle "The Innovation and Technology Venture Fund Corporation" (ITVFC), will co-invest with venture capital (VC) funds selected as Co-investment Partners (CPs) in I&T start-ups with adequate presence in Hong Kong (local I&T start-ups) at an matching investment ratio of approximately 1:2.

Upon an open application exercise for CP selection, ITVF has selected six VC funds as CPs and the list of CPs is available on ITVF's website (https://www.itf.gov.hk/l-eng/ITVF_Partners.asp).

Co-investment Arrangement

2. How would CPs co-invest with the ITVFC?

A "Master Agreement", which sets out the rights and obligations of both parties for co-investment, will be signed between a CP and the ITVFC. Under the agreement, the CP has the obligation to invite the ITVFC to co-invest in local I&T start-ups within a five-year window ("Active Investment Period"). Throughout the Active Investment Period, the CP is responsible for identifying potential investee companies which qualify as Eligible Local I&T Start-ups to the ITVFC for co-investment.

3. What is the eligibility requirements of a local I&T start-up to be selected by a CP for co-investment?

An "Eligible Local I&T Start-up" must meet the following criteria –

(a) it was incorporated under the Companies Ordinance within the last seven years with one of its offices (headquarters or regional office) or its main business operation or its key management or leadership team being located in Hong Kong;

(b) it and its subsidiar(ies) (if any) have been engaging in I&T business, covering any part of the research and development or production chain in Hong Kong; and

(c) it and its subsidiar(ies) (if any) have a total number of employees (including Hong Kong and overseas offices) being less than 250.

4. How about a local I&T start-up being held by a holding company? Will it still be eligible for co-investment?

Yes. If a holding company structure for the chosen local I&T startup is in place, the ITVFC and the CP would invest into this holding company. However, this holding company must only hold and wholly own the chosen local I&T start-up and must not be involved directly or indirectly in businesses not related to the concerned start-up.

5. Whether a local I&T start-up with subsidiaries is eligible for co-investment by the ITVFC and the CP?

An I&T start-up incorporated under the Companies Ordinance of Hong Kong with subsidiaries is eligible for co-investment by the ITVFC and the CP if it meets the eligibility requirements described in the answer of No. 3 above.

6. If a local I&T start-up meets the criteria, can it apply to ITVF directly for investment?

ITVF will be a passive investor, making direct investment in the start-ups concurrently with the CPs upon invitation of the latter. ITVF will **NOT** accept applications or investment proposals submitted by individual start-ups directly.

7. How big will be the co-investment?

The co-investment scheme is targeted at start-ups which are at series A or B stages. Start-ups which are looking for seed funding or pre-series A funding will unlikely be the targets for the co-investment.

8. Will there be any limit on the ITVFC's matching investments?

The ITVFC will set its investment limits as follows –

(a) the aggregate amount of matching investments made by the ITVFC with a CP would not be more than HK$400 million;

(b) the aggregate amount of investments made by the ITVFC with an investee company would not be more than HK$50 million; and

(c) the investment amount made by the ITVFC in each investment deal shall constitute (i) not more than 40% of the original total target of investment sought by the investee company or (ii) HK$30 million, whichever is the lower.

9. Under what circumstances will the ITVFC decline co-investment proposed by CPs?

The ITVFC would decline a proposed co-investment under certain conditions, which include but are not limited to the following -

(a) the proposed investee company is unable to meet the eligibility requirements of a local I&T start-up;

(b) the business of the proposed investee company is in conflict with the existing or planned government policies or legislation; or

(c) there is cause to believe that the proposed investee company may be involved in activities that may bring the Government into disrepute.

10. What are the investment and exit terms for the ITVFC?

The ITVFC will generally co-invest and exit on the same price and terms as the CPs.

11. What will happen if upon the expiry of the Master Agreement, there are co-investments that have not been sold to a third party?

Over the duration of the Master Agreement, a CP should try its best to identify third party buyers to acquire the co-invested shares of the investee companies. However, should there be any shares of the investee companies that have not been sold upon the expiry of the Master Agreement, the investee companies will be required to redeem the shares in their companies from ITVFC should ITVFC decide to exercise the redemption option.

12. What is the investment portfolio of ITVFC?

The updated investment portfolio of ITVFC is available on ITVF website (https://www.itf.gov.hk/l-eng/ITVF_Portfolio.asp).

Incentives and Expenses

13. What incentives will be provided to CPs?

The ITVFC will provide CPs with two incentives. The first one is a carried interest which is equal to 35% of the realised capital gain upon the sale of ITVFC's shares in the investee company to a third party buyer. The second one is an option for the CP to purchase all of ITVFC's shares in all of our co-invested start-ups within the 5-year "Active Investment Period" (*Note*).

Note: Active Investment Period refers to the period within five years from the commencement of the Master Agreement.

14. How could a CP exercise its option to purchase ITVFC's shares of the local I&T start-ups?

During the "Active Investment Period", a CP can exercise its option to purchase all of the co-invested shares in all of the investee companies in which ITVFC has been invited by the CP to invest. When this option is exercised, the CP has to purchase all but not some of the shares of all of the investee companies under the co-investment portfolio. The purchase price is the cost of the principal plus interest accrued for the related investments. The interest rates to be applied for determining the accrued interest are the rates of fee payable by the Exchange Fund to Government funds and statutory bodies for placements which are published by the Hong Kong Monetary Authority for the relevant respective years.

15. **How to calculate the 35% of the realised capital gain to be provided to a CP when the co-investment is sold to a third party?**

Upon the sale of ITVFC's shares in an investee company to a third party buyer, the ITVFC would pay to the CP 35% of the realised capital gain arising from the sale. The realised capital gain would be the net amount of the cash proceeds actually received by ITVFC from such disposal after deducting all cost, fees, expenses, taxes and stamp duty that have been paid or are payable by the ITVFC for such investment.

16. **Will the ITVFC pay CPs any management fees?**

The ITVFC will not pay any management fees to CPs.

17. **What types of costs and expenses arising from co-investment will be shared by the ITVFC?**

The ITVFC will bear all taxes, stamp duties, capital duties and registration fees chargeable by the Inland Revenue Department on the ITVFC arising from the acquisition or sale of the ITVFC's investments. All other costs and expenses incurred by CPs in performing the Master Agreement such as but without limiting to due diligence expenses and all legal costs incurred for the investments would have to be borne fully by CPs.

Termination of the Master Agreement by the ITVFC

18. **Under what circumstances will ITVFC terminate the Master Agreement before expiry?**

The ITVFC will terminate the Master Agreement due to certain events of gross default by CPs, which include but are not limited to, fraud, willful misconduct, gross negligence, violation of criminal law, or breach of the Master Agreement.

19. What are the obligations of a CP when the Master Agreement is terminated by the ITVFC before expiry?

If the Master Agreement is terminated by the ITVFC, the CP must make an offer to the ITVFC to acquire all its stake in all co-invested investee companies. The CP will also be required to provide independent valuation reports on the proposed transaction prices for acquiring the ITVFC's stake in these investee companies.

<u>Enquiry</u>

20. Who should I contact if I want to have more information in relation to the ITVF?

The correspondence address and contact information of the ITVF is as follows –

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