

Research Policies

Consulting

Consulting and Equity Ownership in Start-Up Companies (SC-520)

Scope and Purpose

This policy applies to all HHMI laboratory heads and Senior Scientists. Laboratory heads are Investigators and, at Janelia Farm Research Campus, Group Leaders and Fellows.

Under the [policy on Consulting for Companies](#), laboratory heads and Senior Scientists may not consult for a company in which they own a significant equity interest, which generally means any equity interest greater than 5% of any class of a company's outstanding equity. However, HHMI recognizes that start-up companies typically are established with an expectation that the founders and initial investors will be quickly diluted as the company is capitalized, so that owning an interest of more than 5% of a start-up company's equity at the time of its initial formation does not represent a significant equity interest. The purpose of this policy is to help moderate the impact of the 5% limit on laboratory heads and Senior Scientists wishing to participate in founding and consulting for a start-up company, by providing a "grace period" of up to one year during which the founder or consultant may hold up to 20% of the company's stock in accordance with this policy.

An HHMI researcher who is or will be consulting for a start-up company is referred to in this policy as a "Consultant".

Policy

Service as a Founder is Considered Consulting

HHMI considers a scientist's service as a founder of a company to constitute consulting for the company, and therefore to require prior approval by HHMI, even if there is no written consulting agreement in place. The founders of a company typically perform a range of services for the company, including advising the company on fund-raising and recruiting. This is consistent with HHMI's general view that consulting activities include nearly any service on behalf of a company; see the section on "What is Consulting" in the [policy on Consulting for Companies](#).

Ownership Limits

For a period of one year from the date a Consultant first acquires ownership of any securities of a start-up company for which he or she consults, he or she may own up to 20% of any class of the company's equity securities. Ownership is calculated as described in the policy on [Calculation of Equity Ownership in Companies](#), and in the more technical [Guidelines for Calculating Equity Ownership](#).

Because professional investors such as venture capitalists may be willing to purchase only preferred stock, for purposes of this policy common and preferred stock may be counted as a single class of equity securities if permitted under the policy on Calculation of Equity Ownership in Companies.

In no event may all HHMI Consultants as a group own more than 40% of a start-up company's equity.

By the end of the one-year period (or earlier, if any "significant event", as defined below, takes place), the Consultant's equity ownership must be reduced to not more than 5% of the equity securities of the start-up company.

A "significant event" includes any disposition for profit of company securities by the Consultant, an initial public offering of the company's stock, a sale of all or substantially all of the assets of the company, a merger or consolidation of the company involving a change of control, and any other corporate transaction involving a change of control unless the primary purpose of the transaction is to raise capital for the company's operations.

Anti-Dilution Protection

The 20% exception is intended to provide temporary relief from the strict application of the 5% limit on equity ownership during the early stages of a company, when significant dilution of equity ownership is expected, and serves as a form of anti-dilution protection. A Consultant may not benefit from other forms of anti-dilution protection in addition to the 20% exception.

Accordingly, a Consultant cannot have the right to be "topped up" to 20% if there are rounds of financing during the grace period that reduce his or her interest below 20%, nor can he or she have the right to be kept at 5% or another specific level of ownership after the grace period ends. However, if there is dilution and as a result the Consultant's ownership interest has been reduced to 5% or less, then at that time he or she is free to negotiate additional purchases or grants of equity with the company, so long as he or she does not receive anti-dilution protection and his or her direct and indirect holdings do not exceed 5% of any class of equity as calculated under this policy or the [policy on Calculating Equity Ownership in Companies](#).

Calculation of Equity Interest

In general, a Consultant owns an equity security if he or she, directly or indirectly (for example, through holdings by a member of his or her immediate family or through a trust), has or shares the ability to vote, dispose of or profit from the security or to direct such vote, disposition or profit, or has the right to acquire any such interest at any time.

Please refer to the policy on Calculating Equity Ownership in Companies and to the [Guidelines for Calculating Equity Ownership](#) for detailed guidance on this issue.

Disposition of Excess Holdings

If dilutive events do not reduce the Consultant's ownership percentage of any class of equity to 5% or less by the date that is one year after he or she first acquires ownership of any equity security of the company (or before the occurrence of a significant event as defined above, if the significant event takes place prior to the end of the one year period), then the Consultant will need to dispose of his or her excess holdings by transferring them to the issuing company.

The Consultant may not profit from any disposition of shares to satisfy this requirement. The Consultant must transfer all excess shares to the issuing company so that, after the transfer, he or she owns, directly or indirectly, no more than 5% of any class of equity securities as calculated in accordance with the policy on Calculating Equity Ownership in Companies. The price per share, if any, paid by the company for the excess shares cannot exceed the price per share paid by the Consultant to acquire the shares.

Reporting to HHMI

A Consultant who owns more than 5% of any class of equity securities of a start-up company must provide HHMI with a statement of his or her ownership at the end of the first year following his or her acquisition of any shares (including indirectly through members of his or her immediate family). Each such statement must be signed by the Consultant as well as by a representative of the company. HHMI will endeavor to notify the Consultant when the report is coming due.

Equity Ownership as an Investor Only

A Consultant who is not a founder of a start-up company, and who does not consult for the company in any way (i.e., formally or informally), is not subject to the individual limits on equity ownership in the company. However, the 40% limit on aggregate equity ownership by HHMI laboratory heads and Senior Scientists rule continues to apply.

Thus, if there are HHMI laboratory heads who are founders of a start-up company and own equity, and another HHMI investigator acquires equity strictly as an investor and is not involved as a founder or otherwise in the company, the total ownership of the group still may not exceed 40% of the start-up company's equity.

Procedures Relating to Start-Up Companies

Investigators and host-based Senior Scientists who are contemplating involvement with a start-up company are strongly encouraged to read the [Start-Up Handbook](#) and to contact the HHMI attorney responsible for their site to discuss their plans. Janelia Group Leaders, Fellows, and Senior Scientists may also refer to the Start-Up Handbook, and should discuss their plans with the Janelia Director of Administration and Finance or Chief Operating Officer, who should in turn discuss the proposal with the HHMI attorney responsible for Janelia.

Investigators and host-based Senior Scientists who propose to found or otherwise consult for a start-up company must complete and forward the [Start-Up Questionnaire](#) to the HHMI attorney responsible for their site. The Start-Up Questionnaire identifies a number of related documents that the HHMI attorney will need to review before any consulting agreement can be approved, such as the start-up's business plan and capitalization table.

Please note that HHMI's review of start-up documentation is more involved than the review of other consulting relationships, and thus may take more time to complete than less complicated consulting relationships.

Issued jointly by: Science and Janelia Farm

Issue Date: March 31, 2008