

# Business Incubation

How small businesses can get a head start

*Expert knowledge means success*

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Note: This publication has not been updated since it was last published. Some of the hyperlinks may have changed and may need updating. In addition, some of the information in this publication may be out of date.

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## Introduction

In the Internet-age in which we live, businesses and the transactions they undertake move at the speed of light. For entrepreneurs to succeed they must achieve a rapid speed of execution, particularly with new ideas. Having a good business idea is no longer good enough - getting a business launched around it before a competitor emerges is just as important. Business Incubation can help individuals and their ideas to build successful Internet businesses through reducing the time to market as well as the risk of failure.

The first identifiable business incubator is said to have been launched in Batavia, New York in 1959. It gathered pace, albeit slowly at first, until 1984 when the US *Small Business Administration* (SBA) began strongly promoting incubator development. By then, there were 20 incubators in operation. Over the next few years that number rose rapidly. The *National Business Incubation Association* (NBIA), a US-based private membership organisation of incubator developers and managers, was launched in 1985 by industry leaders with an initial membership of 40 - today, it has grown to almost 800 members.

The statistics for success for start-up firms that commence their life in a Business Incubator are impressive. Several have been so successful that they are large public companies today. Research by UK Business Incubation indicates that business incubators have an average success rate of 98% of businesses succeeding whilst in the incubator (compared to a national average of less than 50% of all small and medium sized companies registered) and 87% surviving after 5 years of starting.

## What is Business Incubation?

Perhaps, if working from home isn't a possibility and you're operating on a limited budget that doesn't allow for you to rent office space, you should consider a Business Incubator - a facility that provides

economical space, plus business services such as typing and copying, some management advice, and possibly financial assistance.

The words "Business Incubation" are used in a number of ways as a generic term to describe several different types of organisation, each offering some form of support to start-up companies:

- Sometimes, this is done in exchange for equity.
- Incubators can include:
  - management advice and business support facilities as well as funding.
  - Venture capital firms offering Service providers (including lawyers, recruitment firms, management consultants, accountants and merchant banks).
  - Product providers such as software developers.

Business Incubators are owned and operated by a wide variety of entities and sponsors, including local government, universities, economic development groups and a combination of other sources. They're located throughout the country, and there's probably one near you. To find the one closest to you, look at the listing we've provided at the end of this publication.

Business Incubation, although not Venture Capital, does contain some elements of that source of funding. Venture Capital is mainly a funding source and only secondly can it provide a source of intellectual capital - this is the "how to" as well as the "what you need is". Business Incubation is different mostly because it can encompass so many things - it's the dynamic process of business enterprise development. Business Incubators nurture young firms, helping them to survive and grow during the start-up period when they are most vulnerable.

Many entrepreneurs find renting office or other space and setting up essential support functions is overwhelming financially and energy-draining just at a time when their financial resources and energy are most needed for development of the business itself. A Business Incubator can be the perfect solution for them

A Business Incubator is a business and financial development tool designed to accelerate the growth and success of entrepreneurial companies through a package of business support resources and service such as:

*"Business incubation is a unique and highly flexible combination of business development processes, infrastructure and people designed to nurture new and small businesses by helping them to survive and grow through the difficult and vulnerable early stages of development."*

*UK Business Incubation Limited*

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- Shared accommodation on a flexible lease basis.
- Flexible office services and equipment, including fee-based business support services, such as meeting room facilities, telephone answering, bookkeeping, secretarial, and fax/copying/printing access.
- Technology support services.
- Business and technical assistance either on-site or through a community referral system.
- Networking with other entrepreneurs
- Assistance in writing a Business Plan and obtaining the funds necessary for the growth of the business.
- Provision of hands-on management assistance.
- Planned exposure to critical business or technical support services.

all of which are usually located under one roof.

The objective of incubation is to produce successful organisations — businesses that are financially viable and freestanding when they leave the incubator usually after two to three years. According to evidence from the US, 30% of incubatee businesses graduate into the outside world each year.

Just as venture capitalists impose selection criteria upon prospective clients, so do Business Incubators. Some accept a mix of industries, but others target industry niches. According to NBIA research, incubator clients may be classified as follows:

- 43% Mixed Use
- 25% Technology
- 10% Manufacturing
- 9% Niche sector
- 6% Service
- 5% Empowerment
- 2% Other

Two principles characterise effective and successful business incubation:

- The incubator aspires to have a positive impact on its community's economic health by maximising the success of emerging companies.
- The incubator itself is a dynamic model of a sustainable, efficient business operation.

Model business incubation programs are distinguished by a commitment to incorporate industry best practices. Management and boards of incubators should strive to:<sup>1</sup>

- Commit to the two core principles of business incubation (see above).
- Obtain consensus on a mission that defines its role in the community and develop a strategic plan containing quantifiable objectives to achieve the program mission.
- Structure for financial sustainability by developing and implementing a realistic business plan.
- Recruit and appropriately compensate management capable of achieving the mission of the incubator and having the ability to help companies grow.
- Build an effective board of directors committed to the incubator's mission and to maximising management's role in developing successful companies.
- Prioritise management time to place the greatest emphasis on client assistance, including proactive advising and guidance that results in company success and wealth creation.
- Develop an incubator facility, resources, methods and tools that contribute to the effective delivery of business assistance to client firms and that address the developmental needs of each company.
- Seek to integrate the incubator program and activities into the fabric of the community and its broader economic development goals and strategies.
- Develop stakeholder support, including a resource network, which helps the incubation program's client companies and supports the incubator's mission and operations.
- Maintain a management information system and collect statistics and other information necessary for ongoing evaluation, thus improving effectiveness and allowing it to evolve with the needs of the clients.

## Which Businesses can be Incubated?

The most common types of firms using business incubators are light manufacturing, technology and service firms and those developing new products or engaged in research and development.

There are a limited number of construction-related, sales and marketing, or wholesale and distribution firms using incubators.

A retail operation is considered a poor fit for incubation.



As the name implies, Business Incubators are designed to nurture small businesses until they are able to exist on their own.

The main benefits are the inexpensive office space and the access to business services.

## Choosing the Right Incubator

In deciding to use a business incubator, the NBIA suggests exploring the following items before making a commitment:

### Space and Service-related Issues

- What are the charges for space and services at the incubator?
- How do those rates compare to market rates locally?
- What services does the incubator provide?
- What are the lease requirements?
- Is there room for your business to grow?

### Quality

- What information does the incubator provide about the extent and quality of the services the incubator provides?
- Does the incubator management seem to understand your business needs and can they offer on-site assistance and access to valuable contacts and community business services needed by your firm?

### Success Rates

- If the incubator has been open long enough to have a track record, what is the experience of firms who made use of the incubator for a few years and have now moved to other space?
- How do the current tenants feel about the incubator?
- Ask for references and check them.

### Policies and Procedures

- What are the policies and procedures of the incubator?
- Are some services provided free of charge?
- How long can you remain a tenant?
- Is there a graduated rent structure as your firm matures or does the incubator want to take royalties or an ownership right in its tenants' businesses in return for reduced charges?
- Can you leave easily if your business gets into financial difficulties?
- Can you leave when you want to? Incubators often protect themselves against a premature termination of the relationship by way of a share buy-back or clawback provision. It's usually contracted that in the case of the start-up wishing to sell its interest to another party, the Incubator must be given the

opportunity to sell its shares at the same price if they want to.

- Are you obliged to sell out if an offer is made for the business - many Incubators argue that the start-up's management team should be obliged to accept a reasonable, bona fide cash offer from a trade buyer, and not hold out in the hope of a £mega-million flotation in the future.
- Does the incubator provide seminar or training programs in addition to other business assistance services?

### Management

- Does the incubator appear to be managed well?
- Does the management appear to have good ties with and knowledge of the business community?
- Does the incubator have the continuing support and commitment of sponsoring organizations?
- Who are these sponsors and what are their goals and reasons for supporting the incubator?



## From the Incubator's Perspective

There are a wide variety of reasons for operating an incubator, such as:

- A need for job creation in the community.
- Promotion of economic self-sufficiency for a selected population group.
- Diversification of the local economy.
- Transfer of technology from universities and corporations or sharing venture experiences with new companies by successful entrepreneurs and investors.

Whatever the reasons behind the incubator, Business Incubators are an economic boon for the community, providing jobs and an expanded business base. They have a wide variety of structures and supportive mechanisms.

You will need to consider whether your business is really ready for this step. The business must be entrepreneurially sound and able to function on its own, if needed. The Business Incubator unit can't replace business initiative, personal effort and resourcefulness. Take care not to fall into the trap of what's called the "incubator syndrome" - in which the entrepreneur allows his/her initiative and judgment to be overtaken by the consultants in the

Incubation unit. Although consultants may give great advice, it must always be your responsibility as the entrepreneur to make the business succeed.

## What else is in it for the Incubator?

A growing trend is for the incubator to receive a piece of the action in exchange for office space, cash and lots of business support. Incubators will take anywhere between 10% and 80% equity in the incubatee, depending on the project's perceived risk, how much of the necessary finance is provided by other sources, and the services or facilities the Incubator offers. Most Incubators take an equity stake of less than 50%, typically between 20% and 40%.

In many ways, the Incubator is becoming a venture capitalist with the benefit of being on site to help get the business off the ground.

## Business Incubators

In the context of the Internet world, Incubators are likely to be the offshoot of an existing venture capital organisation or a dedicated Incubator company. Services that an Incubator might offer include:

- Early stage, seed funding.
- Physical space.
- Process management.
- Managerial involvement.
- Business and back-office support including auditing, accounting, VAT returns and subsidised legal advice.
- Provision of a technical environment, software, hardware, bandwidth and IT support.
- Marketing services.
- Shared development resources.
- Economies of scale.

### If you've got these, you might qualify for Incubation

- A smart, flexible management team
- Large accelerating market
- Unique value proposition
- Sustainable competitive advantage

*WARNING: Entrepreneurs should think carefully before committing themselves to an incubator. Entering into an incubation programme often means a substantial dilution of one's own stake in an existing or proposed business. The flip side is that an incubator could quickly get you to where you want to be and realise an idea that might otherwise not come to fruition - before your competitors beat you to the punch.*

## UK Business Incubation

UK Business Incubation (UKBI) has been the UK's principal and successful authority on incubation, incubation development and good practice since 1998. Its mission is to create successful new UK enterprises and entrepreneurs by leading and promoting the development of high quality business incubation throughout the UK. By providing a dynamic and proactive international hub, through which all their practitioners and stakeholders can engage with them and with each other, they enable vital know-how and good practice to be developed and shared.

UKBI has helped the UK government and regional development agencies to build a thriving business incubation infrastructure including universities, science parks, research and development laboratories, commercial clusters and social regeneration projects.

As business incubation environments mature, UKBI creates and maintains the national network hub for the exchange and development of learning amongst its many communities of interest, including those responsible for developing incubation overseas. More information can be found at: [www.ukbi.co.uk](http://www.ukbi.co.uk)

### The UKBI framework

UKBI have determined that there are 3 stages of business incubation development:

- **Foundation Phase**  
The period of planning, feasibility study, raising finance, marketing, relationship building, and putting together the right management team and Board prior to launch.

During the Foundation Phase, a number of critical elements should be put in place that will define the incubation environment and its offering to and impact on the clients and the wider economy. These key elements include the defining characteristics that make business incubation different to other forms of business support and will provide the cornerstones for the development of the incubation environment over time.

- **Development Phase**  
Following launch, incubation environments will go through a number of developmental phases, which may span many years. It is a time of building up a critical mass and flow of sustainable client companies; building up the services and resources offered to clients; identifying ways in which the incubator can influence the development of the wider economy;



and building a sustainable business model.

- **Cutting Edge**  
The aim for most incubation management teams is to eventually run a high quality, flexible, 'full service' incubation environment that is sustainable in its own right, that has a quantifiable impact on the wider economy, that can be seen to be a catalyst for economic development, and that is creating successful, sustainable ventures. The mature incubation environment may become more specialised, bringing in a full range of advice, support and training opportunities for its clients. It may also be in a position to develop an 'alumni' or support network of past clients as part of the business development network.

### *UK Business Incubation Directory*

New businesses looking for a space in a suitable business incubator now have access to the first UK Business Incubation Directory published on the UKBI website. This A-Z guide provides valuable information on what incubation facilities are out there that could be of help. Details of existing and planned projects are included in the Directory, including addresses and contacts, a brief description of each incubator together with information on total floor space and those which have broadband connectivity.

The Directory is an important indicator of the massive growth and diversity of the business incubation industry and illustrates the broad range of development objectives that it can meet. It is a process that can clearly be applied to the development of high-growth, high-tech firms as well as those contributing to social and economic regeneration and development.

The Directory is available from:

UK Business Incubation (UKBI), Aston  
Science Park, Love Lane, Birmingham B7  
4BJ  
Tel: 0121 250 3538  
<http://www.ukbi.co.uk>

### Other Business Incubator sources

- <http://www.rvc.ac.uk/Enterprise/Incubation/Index.cfm>
- <http://www.i-cocoon.com>
- [http://www.brainspark.com/english/welcome\\_2.phpwww.d2l.com](http://www.brainspark.com/english/welcome_2.phpwww.d2l.com)
- <http://www.sparkventures.com>
- <http://www.idealab.com>
- <http://www.nbia.org>
- <http://www.stockport.gov.uk/services/business/regendevlopment/findingbusinesspremises/stockportbusinessincubator>
- <http://www.sinc.co.uk/home/index.html>

The European Community runs a scheme to certify Business Incubators, of which 160 are gathered under the umbrella of the European Business Network (EBN). You can search a list of EBN members on the EBN website at <http://www.ebn.be/>

### Virtual Incubators

Perhaps expectedly, the Internet has come up with a new breed of Incubator - called Virtual Business Incubators. They are virtual in the sense that, unlike traditional incubators, they don't provide any physical space. Yet, they do provide managerial involvement, networking opportunities, software provision and sometimes seed-funding. With fewer overheads and a wider world-wide-web reach, a Virtual Business Incubator can do more at less cost and if it asks for an equity stake, it will usually be a lower one than is sought by traditional Incubators.

A Virtual Incubator should help you to grow your business through providing a community of expert support business people to share your objectives. Via a web site, the Virtual Incubator provides on-line access to information to help the start-up business to get going.

Typically, services include:

- Accounting - with access to tax data, accounting and audit rules, advice on writing a Business Plan as well as useful templates.
- Outsourcing - of payroll, company secretarial and accounting requirements.
- Company Formation - how to form a company, details of company law, directors' responsibilities and document filing obligations.
- Banking - advice on what's needed to open a business bank account with special arrangements and discounts in some cases for start-up businesses participating in the Virtual Incubator programme.
- Finance - details of financing options on computers, cars and property as well as access to factoring and sales invoice information.
- Insurance - details of what to insure and why, including obligatory insurances such as motor, employers' and public liability, and identifying key risks to insure against such as product liability and key-man insurance.
- Marketing and Sales - what you need to know and do in order to build a marketing and sales strategy and access to all the resources you'll need to do so.



- Personnel - how to recruit, train, motivate and keep people, as well as details of employment legislation.
- Legal - why you need watertight trading terms and conditions plus access to all other legal matters that a new business should know about.
- Business Tools - access to templates and worksheets to make your business life easier and to enable you to assess your progress.
- IT - access to technology experts to advise on computerisation, networking, telephony as well as building your web site and providing e-mail access.

One of the best examples of a Virtual Business Incubator is that of CAPNet Virtual Business Incubator - a web-based small business/micro enterprise counselling and education tool. Look them up at <http://vbi.biz/v2/>

## Virtual Support Networks

Virtual support networks exist online to enable businesses to interact and share ideas and tips for progressing them. They can help you to contact other businesses or organisations within your own specialism or area of expertise that you might otherwise have been unaware of or have been unable to connect with.

Some businesses may prefer to create their own business network for their specialism or industry. There are organisations online that can help you to set up your own e-community, using their contacts and technical expertise. Find out about creating an e-community yourself on the Virtual Business Network website at <http://www.vbnonline.com>

### The Enterprise Europe Network

The Enterprise Europe Network (EEN) provides information and advice to European businesses and entrepreneurs in more than 40 countries. It brings together sellers and buyers of innovative ideas and products. It also aims to help businesses promote new technologies or find new ways to meet a technology need.

There are 11 EEN partner organisations in the UK operating from over 25 different locations. The partner organisations consist of Chambers of Commerce, Regional Development Agencies, universities and other qualified bodies.

### EEN partners work by:

- visiting companies to discuss and assess their needs;
- identifying technologies that could help businesses develop;
- matching companies with suitable European partners or technologies and arranging visits to them;
- helping companies promote their innovative technologies throughout Europe;
- helping companies and research departments make innovative technologies available to each other - technology transfer;
- advising on all stages of technology transfer, including valuing technologies, negotiating contracts, intellectual property and financing.

### More information is available at:

[http://www.enterprise-europe-network.ec.europa.eu/info/services\\_en.htm](http://www.enterprise-europe-network.ec.europa.eu/info/services_en.htm)

### Science Parks

A science park brings together a group of knowledge-based businesses, along with support and advice to help the businesses grow. While the support each science park offers varies, typical services include help with premises, technology expertise and business services that can range from advice on intellectual property to security and cleaning facilities.

Supported through a variety of local, national and European Union programmes, the structure of science parks can vary and there is no common formula for ownership. Universities, local authorities, private companies and property developers can all be involved in different ways and to different levels.

The UK now has over 100 science parks. "Science Park" is the umbrella term used for research parks, technology parks, incubators, innovation centres and technoparks. Different types of Science Park have different aims, for instance:

- an incubator supports new businesses during their early years;
- some science parks specialise in a particular industry, such as biotechnology or information technology;
- a research park may only allow research and development businesses on it;
- Science parks have formal and operational links with centres of knowledge creation, such as



universities, in areas such as technology transfer, sourcing venture capital, student placements and marketing assistance. For example, businesses in the science park can tap into a university's resources and may be able to commercially exploit research being carried out there.

More information about science parks can be found on the UK Science Park Association website at [www.ukspa.org.uk/home](http://www.ukspa.org.uk/home)

### Knowledge transfer schemes

There are two schemes, supported by the Technology Strategy Board, that enable businesses to benefit from the knowledge and experience of other companies and academic institutions.

Small and medium-sized businesses throughout the UK can participate in Knowledge Transfer Partnerships and benefit from the expertise of organisations like further education colleges, universities or research institutes. Recently qualified people at NVQ Level 4 or above are recruited to work in the business as a Knowledge Transfer Partnership Associate. Projects last between one and three years and address product design, manufacturing, product or management processes, computing or management information.

Please ask for our publication on Knowledge Transfer Partnerships:  
[176-Knowledge Transfer Partnerships](#)

Knowledge Transfer Networks are aimed at businesses with specific technical or scientific research and development requirements, which may be eligible for a grant to establish a network through which to share information. The wider business community benefits by being able to access all the knowledge, information and contacts the networks gather. More information is available on the Technology Strategy Board website at <http://www.innovateuk.org/deliveringinnovation/knowledgetransfernetworks.ashx>

The Business Link website can be found at: <http://www.businesslink.gov.uk>

The Enterprise Directorate which is tasked with responding to the needs of entrepreneurs and small businesses can be found at: [www.bis.gov.uk/bbf/enterprise-smes/index.html](http://www.bis.gov.uk/bbf/enterprise-smes/index.html)

The Government provides a number of financial support schemes to encourage innovation and investment including funds and tax reliefs.

## Applying to join a Business Incubation Unit

If you want to apply to join a Business Incubator, the chances are that you will be asked for the following information:

1. Contact Details	
Company name (and trading style if different)	
Postal address	
Contact Name	
Telephone Number	
Fax Number	
E-mail Address	
Web Site Address	

2. What is the outline Business Idea

3. Management Team		
Name	Role and Responsibility	Background Experience

4. Products and Services – what are the products or services you are offering? What will you charge?

5. Marketing Strategy – what media will you use? How much do you plan to spend on marketing?

6. Competition – who else is doing what you are doing? How much are they charging for their products and services? How do you distinguish yourself from them?

7. Key Partners – what partnerships, affiliations or customer relationships are in place? What is the nature of these relationships?

8. Risk Factors – what might prevent you from succeeding?

9. Technology Requirements – what software, hardware, bandwidth, etc. do you need to make it happen?

10. Is a full business plan with at least three-year financial projections available? Who prepared it?

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11. Capital requirements - how much money do you need? How much equity are you offering for this? How much are you putting up yourself?

Amount	£
Equity	%
Your capital contribution	£

12. Income – how will you generate income and from what sources?

Explanation:

Income	Description					Amount
	Product	Service	Units	Customers	Other	
0-12 months						£
12-24 months						
24-36 months						

13. Expenditure - when will you spend your money and on what?

0-12 months	£
12-24 months	£
24-36 months	£

## Does Business Incubation work?

Business Incubators have been used to achieve a wide range of objectives, primarily those that small businesses are good at—creating jobs, developing innovative ideas, diversifying the local economy, and broadly generating activity and wealth by creating a vibrant small business sector.

Business Incubators have an important role to play in supporting local and regional businesses, but entrepreneurs may ask whether they actually work. Over the last 9 years, UK Business Incubation has measured the impact that incubators have on the local economy and workforce. The research proves that an incubator's client businesses provided an average of 167 jobs (full time equivalents) per incubator and are home to an average of 30 client businesses. Most (60%) incubators also operate "outreach" services, helping and advising companies outside the incubator. Those operating outreach activities support an average of 150 additional businesses. Across the sample, an average of 75% of client **companies' turnover up** to £500,000, but only 1.5% had a turnover of > £5 million.

Most importantly, business incubators have an average success rate of 98% of businesses succeeding whilst in the incubator (compared to a national average of less than 50% of all small and medium sized companies registered) and 87% surviving after 5 years of starting.

Source: UKBI

## Further Information

This guide is for general interest - it is always essential to take advice on specific issues.

We believe that the facts are correct as at the date of publication, but there may be certain errors and omissions for which we cannot be responsible.

If you would like to receive further information about this subject or other publications, please call us – see our contact details on the next page.

### References

<sup>1</sup> Developed by NBIA, with credit to the book, Growing New Ventures, Creating New Jobs: Principles and Practices of Successful Business Incubation, Rice M. and Matthews J., 1995.

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