From: Jerome Soller [soller@cognitech-ut.com]
Sent: Friday, April 01, 2005 2:48 AM
To: restructure.sizestandards@sba.gov
Cc: julie.slocum@mail.house.gov
Subject: RIN 3245-ZA02 Opposition to Proposed Exception for Small Business Size Standards for VC Companies

Dear Small Business Administration,

I am writing this e-mail to express my strong opposition to the attempts to bypass the letter and spirit of small business size regulations, titled, "Participation of Businesses Majority-Owned by Venture Capital Companies in the SBIR Program" in the SBA's December, 2004 Advanced Notice of Proposed Rulemaking. My small business is located in Salt Lake City, Utah, and specializes in software research applied to healthcare information systems and homeland security (e.g., detection and response to terrorist attacks). We have discussed this issue with many other Utah-based small businesses, who all believe that this effort will lead to the disappearance of many independent small businesses and the jobs they support. We have also presented our views one year ago to staffers for Congressman Bennett, Hatch, and Matheson of the State of Utah. We are distressed that this proposal has resurfaced again!

At this time, 97.5% of federal Research & Development money can be pursued by entities including large not-for-profit laboratories (e.g., Battelle), universities, large corporations, and companies owned by large VC companies. The reality of the way these programs are structured is that it is very difficult for small companies, particularly emerging small companies, to win these grants and contracts, given the political connections and resources of their larger competitors (regardless of technical innovation). We have experienced these roadblocks many times. The 97.5% of federal biotechnology grants and contracts funded outside the SBIR program are dominated by large companies, universities and other organizations who are not independent small businesses. The SBIR program only represents 2.5% of all federal R&D, which gives small companies a chance to establish themselves and introduce innovation. Instead of further eroding a program to help independent small businesses, Congress should focus their energies on evening the playing field for these other opportunities and facilitating the award of Phase III opportunities and other technology commercialization that builds on SBIR-funded technologies.

Second, there is nothing magical about VCs that they should deserve special treatment to ignore the size standards. If special exceptions are granted to VCs, there is no compelling reason to deny similar treatment for banks, retirement funds, universities, not-for-profit organizations, and large companies. Once they consider special exceptions for VCs, every lobbyist for other organizations will ask for the same consideration. Can you imagine the complexity for the SBA to try to create and interpret rules/special exceptions for this kind of change in the regulation? The net result for any kind of special exception of the size standards is an erosion of the ability of the SBIR program to support innovation. Small businesses with ten people would find themselves competing against pooled VCs that share proposal writing teams and other resources across many proxy (not independent) "small" companies. Entrepeneurs would be pressured to sell their ideas to VCs to have any chance to pursue federal funding. VCs could buy up many companies in certain areas, reducing competition and flooding a given RFP topic with multiple responses from companies they own. Even if these other organizations could not directly own small businesses, they could control the VCs that own the small businesses. It would remove incentive for universities to team with independent small businesses. Instead, they would only have financial incentive to team with companies they own or indirectly control. For example, the University of Utah may be allowed to own portions of small businesses in the future. However, many independent small Utah businesses are concerned about the possibility that the university could own proxy small businesses outright and compete against them (instead of teaming with them, as they do now). Large companies (e.g., manufacturers, prime system integrators at Dugway Proving Ground) would award Phase III SBIR contracts to proxy small businesses they control, leaving independent small businesses with less opportunities to transition their SBIR-funded technologies.

Third, the term "biotechnology" is vague. For example, my company develops software for the modeling and simulation of chemicals, materials, and chemical detectors. One could argue that we and a wide variety of companies are "biotechnology" companies. The term could mean many things to many people, and will be stretched to its largest possible scope, until the distinction with other areas becomes meaningless. At a later point, every other major discipline will ask for the same exception. Furthermore, why would the biotechnology area ask for special VC exceptions to the size standard? These VC-owned biotech companies currently have the ability to pursue the 97.5% of NIH, HHS, NSF, and DoD heath-related R&D funds for biotechnology with much greater resources than their small business competitors.

Fourth, there is nothing magical about the SBIR program that would make size exceptions justifiable. Once exceptions are made here, I expect to see the same lobbyists push for changes in other small business setaside or incentive programs, including loans, 8a, etc. By similar logic, they will argue that if a large VC owns a company that has one employee who is an American Indian, they should be considered an 8a company. VCs will receive special treatment to bypass the spirit of small business programs, at the expense of independent small businesses.

In summary, we see no sound reason to provide special privileges to the VC-owned entities to be exempt from the size standard. If such changes are made, the result will be chaos among interpreting special exceptions, a large number of independent small businesses ceasing to exist, and a reduction in innovation and diversity among those that survive.

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