



Testimony of

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**BEFORE THE COMMITTEE ON SMALL BUSINESS AND ENTREPRENEURSHIP  
UNITED STATES SENATE**

**Washington, D.C.**

**“Strengthening the Participation of Small Businesses in Federal  
Contracting and Innovation Research Programs”**

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*SBTC, the nation's largest association of small, technology-based companies in diverse fields, is proud to serve as the technology council of the National Small Business Association, the nation's oldest nonprofit advocacy organization for small business, serving more than 150,000 small companies throughout the United States.*

Madam Chair Snowe, Senator Kerry, members of the Committee, good morning. I am Michael Squillante, Vice President of Research of Radiation Monitoring Devices, Inc., in Watertown, Massachusetts and Chairman of the Small Business Technology Council, the technology council of the National Small Business Association. Thank you for inviting me to appear here.

Radiation Monitoring Devices was founded in 1974 to perform research on high performance sensors, which now includes nuclear, optical biochemical and magnetic sensors. RMD also develops and manufactures commercial products based on these sensors for medical and industrial use. Presently RMD's research is focusing on the next generation of instruments for cancer diagnosis, homeland security and nondestructive testing.

The Small Business Technology Council was founded in 1995 to represent small, technology-based firms. Today such companies employ over half of the nation's scientists and engineers,<sup>1</sup> and produce about *13 times* more patents per employee than large patenting firms.<sup>2</sup> These patents are twice as likely as large firm patents to be among the one percent most cited in scientific and technical literature and in subsequent patent applications.<sup>3</sup> Small firm innovation is twice as closely linked to scientific research as large company research, on average, and is thus substantially more "high tech" or "leading edge."<sup>4</sup>

By almost all objective accounts, including studies by the Government Accountability Office<sup>5</sup>, the National Academy of Engineering<sup>6</sup>, and the National Academy of Sciences<sup>7</sup>, the federal government's most successful effort to encourage and sustain these smaller technology companies has been the Small Business Innovation Research (SBIR) Program.

Progenitor of an astonishing 45,000 patents and tens of billions of dollars in economic activity, this remarkable Program is coming up for re-authorization by Congress soon. We hope that today's hearing marks the beginning of a comprehensive examination of SBIR by this

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<sup>1</sup> *Science and Engineering Indicators 2006*, National Science Foundation. See [www.nsba.biz/docs/tibbetts\\_sbir\\_reauthorization.pdf](http://www.nsba.biz/docs/tibbetts_sbir_reauthorization.pdf)

<sup>2</sup> *Frequently Asked Questions*, U.S. Small Business Administration, June 2006, [www.sba.gov/advo/stats/sbfaq.pdf](http://www.sba.gov/advo/stats/sbfaq.pdf)

<sup>3</sup> *Small Serial Innovators: The Small Firm Contribution To Technical Change*, CHI Research, Inc, under contract to the U.S. Small Business Administration, March 2003, [www.sba.gov/advo/research/rs225tot.pdf](http://www.sba.gov/advo/research/rs225tot.pdf).

<sup>4</sup> *Ibid.*

<sup>5</sup> *Federal Research: Assessment of Small Business Innovation Research Programs*, GAO Report RCED89-39, January 23, 1989; *Federal Research: Small Business Innovation Research Program Shows Success But Could Be Strengthened*, GAO Report T-RCED 92-3, October 3, 1991; *Federal Research: Interim Report on the Small Business Innovation Research Program*, GAO Report 95-59, March 8, 1995; *Federal Research: Observations on the Small Business Innovation Research Program*, GAO Report RCED 98-32, April 17, 1998; *Federal Research: Observations on the Small Business Innovation Research Program*, GAO Report GAO-05-861-T, June 28, 2005.

<sup>6</sup> *Small Business Innovation Research Program: Challenges and Opportunities*, Board on Science, Technology and Economic Policy, National Academies of Science and Engineering, 1999.

<sup>7</sup> *Conflict and Cooperation in the National Competition for High Technology Industry*, National Academy of Sciences, 1996; *SBIR: Assessment of the Department of Defense Fast Track Initiative*, STEP Board, National Academies of Science and Engineering, 2000. Another National Academy of Sciences study of the SBIR Program is ongoing, with a final report expected late in 2006.

Committee, as well as timely re-authorizing legislation. In that light, we commend to the Committee a recent analysis of SBIR by Dr. Roland Tibbetts, the “father” of the Program.<sup>8</sup>

### Five Principles

SBTC believes that SBIR owes its success to five central principles.

1. The SBIR Program does not “pick winners” that it foresees as “creating new industries” or generating blockbuster performance in the private sector. SBIR contracts are awarded to meet the *federal government’s own research needs*, as stated in published research solicitations. While SBIR technologies that go beyond Phase 1 are expected to be commercializable, neither the federal government nor the SBIR Program Managers attempt to guess which technologies will spawn the “great industries of the future.”

2. The contract award process is *transparent and competitive*. Any small business may submit a proposal attempting to address the research needs that the government has publicly described. But a scientifically rigorous – and equally transparent – evaluation process helps assure that only the most promising proposals receive awards.

3. The SBIR Program is structured into “*Phases*” that align with the natural evolution of an innovation through research and development. Phase 1 SBIR Awards aim at the “blank sheet of paper” stage of research – developing and proving theoretical technological solutions to problems. Phase 2 Awards move these proven solutions along toward working prototypes. And Phase 3 Awards shift the work toward the “real world” through commercialization – whether by having the government itself purchase the products (as agencies like the Defense Department do) or by having the private sector purchase and diffuse them to meet public needs (as agencies like the National Institutes of Health do).

4. The SBIR Program is designed to – and generally does – carefully *protect the intellectual property rights of the scientists and inventors* that it seeks. That protection assures a continuing flow of the small business community’s – and many of the nation’s -- top scientists and technologists into innovation challenges that the federal government faces. Yet it avoids both the direct costs of a growth in federal employment and the indirect costs of removing these talented individuals from the private sector.

5. Perhaps most importantly over the long run, the SBIR Program is built on a *recognition of the different research styles and capabilities of large and small businesses*.<sup>9</sup> At exactly the early stages of R&D where small companies have historically been the most productive producers of technological breakthroughs, they, and only they, can access SBIR research awards. These small companies are not required to compete with universities or large businesses for their contract awards. They compete only with one another, and on a level playing field. At the *later* stages of R&D where large company financial support, manufacturing expertise and marketing muscle is vital – corresponding to Phase 3 of SBIR – such companies are welcomed into the Program. Indeed, they are indispensable to its success.

These principles can help us put today’s discussion in context.

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<sup>8</sup> This paper can be accessed from the SBTC website, at [www.nsba.biz/docs/tibbetts\\_sbir\\_reauthorization.pdf](http://www.nsba.biz/docs/tibbetts_sbir_reauthorization.pdf)

<sup>9</sup> See William J. Baumol “Entrepreneurship, Innovation and Growth: the David-Goliath Symbiosis”, *Journal of Entrepreneurial Finance and Business Ventures*, Vol. 7, Issue 2, Fall 2002, pp. 1-10.

Turning now to the proposed change in the SBIR Program, I will suggest some insights based on SBTC's experience with the Program, and that of my company.

### **SBTC's Background**

More than three hundred of SBTC's member companies that have won SBIR contract awards from different agencies of the federal government. So have scores of former SBTC member companies that have been merged or acquired by other firms. No organization in the United States represents as many current and former SBIR contract awardees. Using this "intellectual capital," SBTC has been closely involved in the development and reauthorizations of the SBIR Program for over a decade. SBTC's Executive Director was a principal architect of the original SBIR legislation in 1982.

### **RMD's Experience with SBIR**

With a major assist from SBIR contract awards at key points in our history, my company – RMD -- has grown from 12 employees to 80 and has spun off six new high technology companies. More importantly, SBIR funding, and in particular SBIR funding from the National Institutes of Health (NIH), has allowed us to carry out research and development that improves the quality of life of tens of thousands of people in a many ways, from making possible better surgical outcomes and faster post operative recovery to helping insure homes are free of lead which still affects hundreds of thousands of children in the United States. For example, an NIH SBIR grant carried out by RMD in collaboration with Dr. David Stump at the Wake Forest University School of Medicine changed the way open heart surgery is performed, resulting in an order of magnitude reduction in the incidence of stroke following surgery.

### **Our Concerns**

I am here today because of SBTC's and my company's serious concern that some proposals for fundamental change in this vital small business program will make it much harder for small firms to produce significant life science innovations in the future.

Venture capital companies are the crux of the issue.

Currently, VC's of any size may control up to 49% of SBIR companies. And VC's that are *small* by SBA and SBIR statutory standards (fewer than 500 employees, including affiliates and subsidiaries) may control up to 100% of SBIR companies.

The dispute centers on what *large* VC's will be permitted to do. Some elements of the biotechnology and venture capital industries want to allow venture capital companies that are *large* by SBA and SBIR statutory standards to own or control small companies that receive SBIR contract awards.

*Such an action would breach the SBA affiliation rule – something that has never occurred in the fifty-three year history of the Small Business Act and the Small Business Administration. It would also breach SBIR's statutory definition of a small business, established by Congress nearly 25 years ago and ratified at least four times since.*

Proponents say that this dramatic change is necessary to assure small life science companies with the outside capital they need to grow.

We disagree. Not only is it unnecessary; it is detrimental to SBIR.

We believe this change, if implemented, would:

1. Make SBIR awards at NIH both less competitive and less transparent.
2. Undermine the character of NIH's Phase 1 Awards as early-stage R&D.
3. Reduce, probably dramatically, the number of NIH SBIR awards and the number of recipient companies.
4. Short-circuit SBIR Phase 3, Congress' intended locus for partnerships between large and small companies.
5. Inexorably shift the NIH SBIR focus away from a pure expression of the agency's own research needs and toward the preferences of large venture capital company investors.
6. Crowd out many small life science and biotechnology companies with important innovations.
7. Go against the strong preferences of current SBIR awardees at NIH.
8. Duplicate the funding that is already available through other NIH channels to biotechnology firms that are owned or controlled by large VC's.
9. Further concentrate SBIR awards in a few states.
10. Raise questions about whether SBIR is truly a small business program.
11. Create dangerous legal precedents that could threaten not only the SBIR Program, but most other federal small business programs.

### Competition

The selection of SBIR awardees at NIH is based on a scoring system. Proposals score well when they include items like preliminary research results, well-credentialed teams, and connections to other ongoing research related to the topic. A company with access to deep-pocketed VC's will be able to afford all this and more. Not only can such a company develop preliminary research, assemble impressive teams, and gain access to related research. It can also afford to submit *multiple* proposals for each research topic – and to assemble all of its proposals into far more polished packages than small start-up companies can afford. In time, these advantages will sharply tilt the playing field toward SBIR proposals backed by large VC's. The companies that are crowded out will be exactly those “diamonds in the rough” that the SBIR Program was intended to identify and nurture. Moreover, these large VC-backed firms are primarily interested in *high-dollar* awards that NIH has been making in violation of the SBIR Program Guidelines.<sup>10</sup> Since the dollars available in the SBIR Program are capped, these high-dollar awards are reducing the total *number* of SBIR awards available. Insert large VC's into this situation and smaller companies will get a “double whammy.” Not only will they be competing against rivals financed by large VC's, but they will also be competing for fewer awards.

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<sup>10</sup> According to GAO, over 50% of NIH's recent SBIR awards exceeded the Program Guidelines published in the Federal Register. See *Small Business Innovation Research*, GAO report 06-565, April 2005, p.5

## Transparency

Under the current SBIR system, the identities of SBIR awardees are not only known, but a matter of public record. Those seeking to change the SBIR Program want this safeguard ended. They seek to eliminate SBA's requirement that SBIR companies, and any VC's that control them, be owned by individuals rather than institutions. The net effect of doing this would be to obscure exactly who, or what institutions, would derive the ultimate benefits from an SBIR award, including any resulting intellectual property. The true beneficiaries could turn out to be the same universities and large companies that *already* dominate federal R&D contracting. Yet the SBIR Program was created to address precisely this imbalance.

## The Integrity of Phases 1 and 3

One key reason SBIR works, as noted, is that it funds R&D in steps. That also is at risk here.

Phase 1 SBIR awards, intended for very early-stage research, give agencies like NIH a competitive, rigorous, and scientific process for singling out meritorious ideas and developing them. But early-stage R&D funds like SBIR Phase 1 awards are quite scarce in both the private and public sectors. At NIH today, for example, only about one out of every eleven Phase 1 proposals is funded. The awards are in the hundreds of thousands of dollars, not the millions. Any loss of focus in NIH's Phase 1, or reduction of available funds, will have significant repercussions on early-stage, life science R&D because there are so few funding alternatives.

SBIR Phase 3 is quite different. It is explicitly intended for R&D *output* -- products nearing commercialization. Phase 3 is predicated on partnerships between SBIR companies and others, such as large businesses. VC's of any size may partner with SBIR companies in Phase 3.

Phase 3 access, evidently, is not enough. What the large VC's now seek is *Phase 1* access.

There are major problems with this.

- *NIH and VC priorities for basic R&D differ dramatically.* In the life sciences, the VC business model emphasizes innovations that have wide applicability, are close to commercialization, look likely to receive FDA approval, promise rapid triple-digit paybacks, and will be used by patients over a period of months or years. (Not incidentally, these are also the factors that most interest Wall Street.) In general, life science VC's have been very interested in "blockbuster drugs" and medical devices, but not much else. Yet much of the NIH public health and homeland security mission is devoted to other priorities – like biodefense, vaccine development, diagnostics, platform technologies, research tools, orphan disease therapies, agricultural biotechnology, and environmental biotech. An aggressive push by large VC's into Phase 1 will -- at minimum -- create a lot of friction over such priorities. Over time, it will lead to great pressure on NIH to adapt research solicitations to VC preferences.
- *What VC's really want is incompatible with Phase 1.* Here's a recent analysis of this point from the biotech trade press:

**"The biotech industry seems to be at a crossroads ... With the focus now on developing products that are already in clinical development ... biotech investors now seem to be more risk adverse. Their investment strategy is to focus on investing in**

**companies with products in late stages of clinical development, which they believe will receive FDA approval.” (Emphasis added)<sup>11</sup>**

Virtually nothing in SBIR Phase 1 fits this description. Virtually everything in Phase 3 does. And the VC and biotech communities seem to know it.

Here’s a speaker from a venture capital panel at a recent Biotechnology Industry Association general meeting:

“‘In the late 1990s, investors were willing to back early-stage technology phases of biotechnology,’ said Jim Barrett, an analyst and general partner of New Enterprise Associates. ‘Now the investment community is moving toward later-stage projects. That means that early-stage projects are having difficulty raising money in this environment of risk discounting.’”<sup>12</sup>

This raises a very interesting question: why do the big VC’s want in to Phase 1?

The most logical answer is that they want access to the increasingly large NIH SBIR awards<sup>13</sup> -- and that they intend to bend the entire SBIR Program at NIH to their preference for later-stage research.

SBTC believes that Congress should not be a party to any such unraveling of the SBIR Program.

### **Alternative NIH Funding Channels Available to Larger Companies**

NIH has a variety of grant and contract programs that draw on the *97½% of its extramural research funding that is not allocated to SBIR*. And over 40% of NIH funding now goes to applied, as opposed to basic, research.<sup>14</sup> These programs do not require an applicant company to be small. Among them:

- *Exploratory/Developmental Research Grants (R21)*. These support pilot-scale studies for potentially ground-breaking ideas, methods, and systems that meet the following criteria: they lack sufficient preliminary data, their successful demonstration would have a major impact on biomedical research, and they fall within the areas supported by the awarding institute. A second stage of the R21 grants, R33 grants, is parallel to SBIR Phase 2. These grants are rising rapidly. At the National Cancer Institute, which is the largest of the National Institutes of Health, R21’s have risen from 34 grants, valued at \$7.6 million in 1995 to 425 grants, valued at \$77.9 million in 2004. Meanwhile, R33’s, which began in 1999 with 6 grants valued at \$2 million, have risen to 96 grants, valued at \$42.9 million in 2004.<sup>15</sup>

<sup>11</sup> “Wall Street Biobeat” John Wong, Ph.D., *Genetic Engineering News*, March 1, 2005, p. 60.

<sup>12</sup> “Investors: Show us the Drugs,” *Business Gazette*, June 24, 2005

<sup>13</sup> This is especially remarkable in view of the **\$53.6 billion cash hoard** of funds held by venture capital companies in 2005 but not invested in venture projects. See “Overhang of Venture Capital Funds at \$53.6 Billion” Dow Jones / VentureOne Press Release, March 24, 2005. [www.ventureone.com/ii/V1-FundsOverhangSurvey2005.pdf](http://www.ventureone.com/ii/V1-FundsOverhangSurvey2005.pdf) Note, too, that over half of NIH’s awards exceed federal guidelines, a major enticement to the VC’s. See footnote 10.

<sup>14</sup> “NIH at the Crossroads: Myths, Realities and Strategies for the Future,” Elias A. Zerhouni, M.D., Director, National Institutes of Health, May 22, 2006 presentation, NIAID Council., p. 5

<sup>15</sup> *NCI Fact Book 2004*, National Cancer Institute, 2005, P. E-3

- *Individual Basic Research Grants (R01)* are awarded to eligible institutions/organizations on behalf of a principal investigator to support a discrete hypothesis-driven research project related to the investigator's area of interest and competence.
- *Program Project Grants (P01)* are more complex in scope and budget than the individual basic research (R01) grant. While R01s are awarded to support the work of one principal investigator who, with supporting staff, is addressing a scientific problem, program project grants are available to a group of several investigators with differing areas of expertise who wish to collaborate in research by pooling their talents and resources. Program project grants represent synergistic research programs that are designed to achieve results not attainable by investigators working independently.
- *Small Research Grants (R03)* support small research projects that can be carried out in a short period of time with limited resources for projects such as pilot studies; secondary analysis of existing data; small, self-contained research projects; and development of research methodology. R03 grants often are used as a stepping stone to a new investigator's first R01 grant.

A good example of the parallelism that is developing between the SBIR awards and the “Exploratory / Developmental Research Awards” (R21) awards can be seen in two recent NIH solicitations bearing the same title: “Development of Advanced Genomic Characterization Technologies” – one an SBIR solicitation and one an “R21”.<sup>16</sup> The solicitations are nearly identical.

SBTC urges the venture capital and biotechnology communities to work with NIH in developing these promising channels of research funding that do not impinge on the SBIR Program.

### SBIR Awardee Preferences

Proponents of large VC control of SBIR companies have argued that they were responding to pleas from the SBIR companies themselves. Since we at SBTC had heard only *criticism* of the proposal from our member companies, we wondered about that. So we took a survey.

We contacted every NIH SBIR Phase 1 and Phase 2 awardee from 2003 and 2004. We sent them a link to a position paper *favoring* the change that was posted on the Biotechnology Industry Association (BIO) website, and a link to a position paper *opposing* the change that was posted on our website. We asked the companies to read the two position papers and then vote on whether to support or oppose the change.

Just over 13% of the companies replied – not a bad response rate in view of the time required to read the two position papers.

Of these, 90% opposed the VC eligibility change advocated by BIO.

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<sup>16</sup> The R21 solicitation will be found at: <http://grants.nih.gov/grants/guide/rfa-files/RFA-CA-07-021.html> . The SBIR solicitation will be found at: <http://grants.nih.gov/grants/guide/rfa-files/RFA-CA-07-029.html>

This result speaks for itself: *The companies most affected by the proposed change, who theoretically stand to gain from it, are overwhelmingly opposed to it.*

And that's not all. At a large conference on SBIR Phase 2, speakers advocated both sides of the issue, after which a written ballot was taken of attendees. The vote count was 1 in favor (the speaker in favor, presumably) and 149 opposed.

In my own state, the respected New England Innovation Alliance has strongly opposed these changes.<sup>17</sup>

SBTC's 19-member Board of Directors voted *unanimously* to oppose the large VC position in 2003. From then, through today, *not one single SBTC member company* has voiced an objection to our position. In fact, we have attracted a number of small biotech companies to SBTC membership *because of* our opposition to the VC position.

### **Harvesting Innovations From All Regions of the Country**

Allowing large VC's to control SBIR companies also would be likely to further concentrate SBIR awards around Boston and the San Francisco Bay area, where many VC's are headquartered and where they make 58% of their investments. While I myself come from the Boston area, it's apparent to me that Congress meant for the SBIR Program to attract the widest possible swath of applicants, from all across the country. Indeed, that's why Congress created the Federal and State Technology Partnership (FAST) Program and the SBIR Rural Outreach (RO) Program.

But today ten states account for 85% of all VC investments. Despite the 750-850 venture capital deals done annually in the U.S., at least a dozen states received two or fewer of them annually for most of the past ten years. That list includes Maine, Montana, South Dakota, Louisiana, Wyoming, Iowa and Arkansas.<sup>18</sup> Likewise, none of the 100 largest VC's were located in thirty-one states. And only two percent of venture capital goes to seed and early stage investment -- the type SBIR companies need most.

At the Maryland Technology Development Center in Rockville, MD, a county-operated facility that houses perhaps the largest concentration of small biotech firms in the mid-Atlantic region, *not a single biotech company* has raised a first round of venture capital during the past five years -- but most have successfully competed for SBIR Phase 1 and 2 contract awards. Tilting the SBIR playing field against companies like these -- who have not the slightest prospect of VC funding -- will guarantee that many of them will disappear. When they go, their potential life science innovations will likely go with them.

### **Avoiding Potentially Dangerous Legal Precedents**

Contravening SBA's affiliation rule, and SBIR's statutory limit on the size of businesses that can access the Program, carries with it significant legal risks.

Large corporations like the Bank of America and Intel already operate their own venture capital companies. Not only would such "corporate" VC's enter the SBIR Program if SBA's affiliation

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<sup>17</sup> Accessible at [www.nsba.biz/docs/nea\\_letter.pdf](http://www.nsba.biz/docs/nea_letter.pdf)

<sup>18</sup> See *Money Tree Venture Capital Profile for the United States*, [www.ventureeconomics.com/vec/stats/2006q1/nation\\_us1.html#state](http://www.ventureeconomics.com/vec/stats/2006q1/nation_us1.html#state) and PriceWaterhouse Coopers Money Tree Report, [www.pwcmoneytree.com/moneytree/nav.jsp?page=historical](http://www.pwcmoneytree.com/moneytree/nav.jsp?page=historical)

rules are changed, but the incentive for other corporations to *create* more such VC's would dramatically increase. Corporations like Boeing, Genetech, Lockheed Martin, Microsoft, and the large pharmaceutical firms could be expected to form venture capital companies for this explicit purpose. Soon small companies competing for SBIR awards throughout the government would find themselves fighting with Fortune 500 corporations for the small SBIR share (2½%) of federal R&D dollars.

It would be unlikely to end there, either. Once such large corporations have broken through the legal framework that has kept them out of the SBIR Program, there would be no equitable argument for keeping universities and other large research institutions from participating in the SBIR Program via *their* own VC's.

Stepping a bit further back, if SBA waives its affiliation rules in this situation – for the first time in the fifty-three year history of the agency and the Small Business Act – it would open up every other small business program in the nation to challenge.

If large companies can force their way into the SBIR Program, why should they be kept out of the SBA's other federal procurement programs, its 7(a) lending program, its Small Business Investment Company program, its surety bond guarantees? Why should SBA's Office of Advocacy continue to distinguish between large and small companies in its efforts to reduce the federal regulatory burden?

The implications of this proposed rule thus transcend the SBIR Program itself, federal R&D contracting, or even overall purchasing practices by the federal government.

The real nub of the issue is whether a large business can take over a small business and still get the federal government to call it "small." If Microsoft controls and funds Sam's Computer Repair, is Sam's a "small business" or a part of a large business?

Sooner or later, the public will come to see it in these terms.

At heart, then, this is simply a classic dispute between small business and big business.

***What a few large companies seek here is nothing less than a breach of the single most fundamental principle of federal small business law: that a small business is one which is "independently owned and operated".*** That was the language used in the Small Business Act over half a century ago, and it is the foundation upon which dozens of subsequent laws, and hundreds of subsequent regulations, are built.

Contravening this principle, with all the legal risks that entails -- to allow a handful of companies to access SBIR funding at one agency -- is surely not what Congress and the American people intend for the nation's canon of small business laws and protections.

SBTC strongly urges Congress to be vigilant in discerning the long-term consequences of any actions in this legal area.

## Need For Change Not Established

Perhaps some of these concerns could be set aside if the need for this change were more clearly established. That hasn't happened. On the contrary, key assertions made by the proponents of the change have been *disproven* in a recent GAO report.<sup>19</sup>

- ***Proponents say the number of SBIR awardees at the National Institutes of Health (NIH) with VC backing is dropping.*** GAO says the number is **up** more than **50%** since SBA clarified its long-standing rules on VC's in 2002. Phase 2 awards are up over **70%**.
- ***Proponents say the quality of SBIR research at NIH is dropping.*** GAO data suggest otherwise. Despite increasing budgets at NIH, the rapidly rising number of applicants permitted NIH to become far more selective in its awards.<sup>20</sup>
- ***Proponents say VC-backed companies are getting fewer dollars from SBIR awards at NIH.*** GAO says VC-backed firms now account for more than \$1 out of every \$5 that NIH awards. That's up more than 50% over three years.
- ***Proponents strongly imply that the SBIR Program at NIH isn't working.*** Numerous studies, cited earlier, by GAO, the National Academy of Sciences, and other independent organizations say the Program is successful.

And one more thing.

- ***Proponents say that NIH endorses the changes they seek.*** In a letter to SBA Administrator Hector Barreto dated 28 June 2005, NIH Director Elias Zerhouni stated that NIH wished to award SBIR funds only when "*applicable small business affiliation standards are satisfied.*" In a second letter, to Anu K. Mittal of GAO (who directed the above study), dated 16 June 2006, NIH Deputy Director of Extramural Research Norka Ruiz Bravo repeated NIH's concern that "*applicable small business affiliation standards are satisfied*" in any changes affecting the NIH SBIR Program. The letter then reiterated that:

"NIH is committed to insuring that only *small* business concerns receive SBIR awards."  
(*Emphases in originals.*)

**For these reasons, SBTC asks Congress to maintain the prohibition in the SBIR Program against venture capital company control of SBIR contract awardees when the VC's involved do not meet the current legal definition of a small business.**

<sup>19</sup> *Small Business Innovation Research*, GAO Report 06-565, April 2006

<sup>20</sup> *Ibid.*, Tables 21 and 22, page 38.